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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 37

W. G. WELBON, E. N. CLAUGHTON and
A. W. CORBETT,
Petitioners,

vs.

ATLANTIC COAST LINE RAILROAD COMPANY,
Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

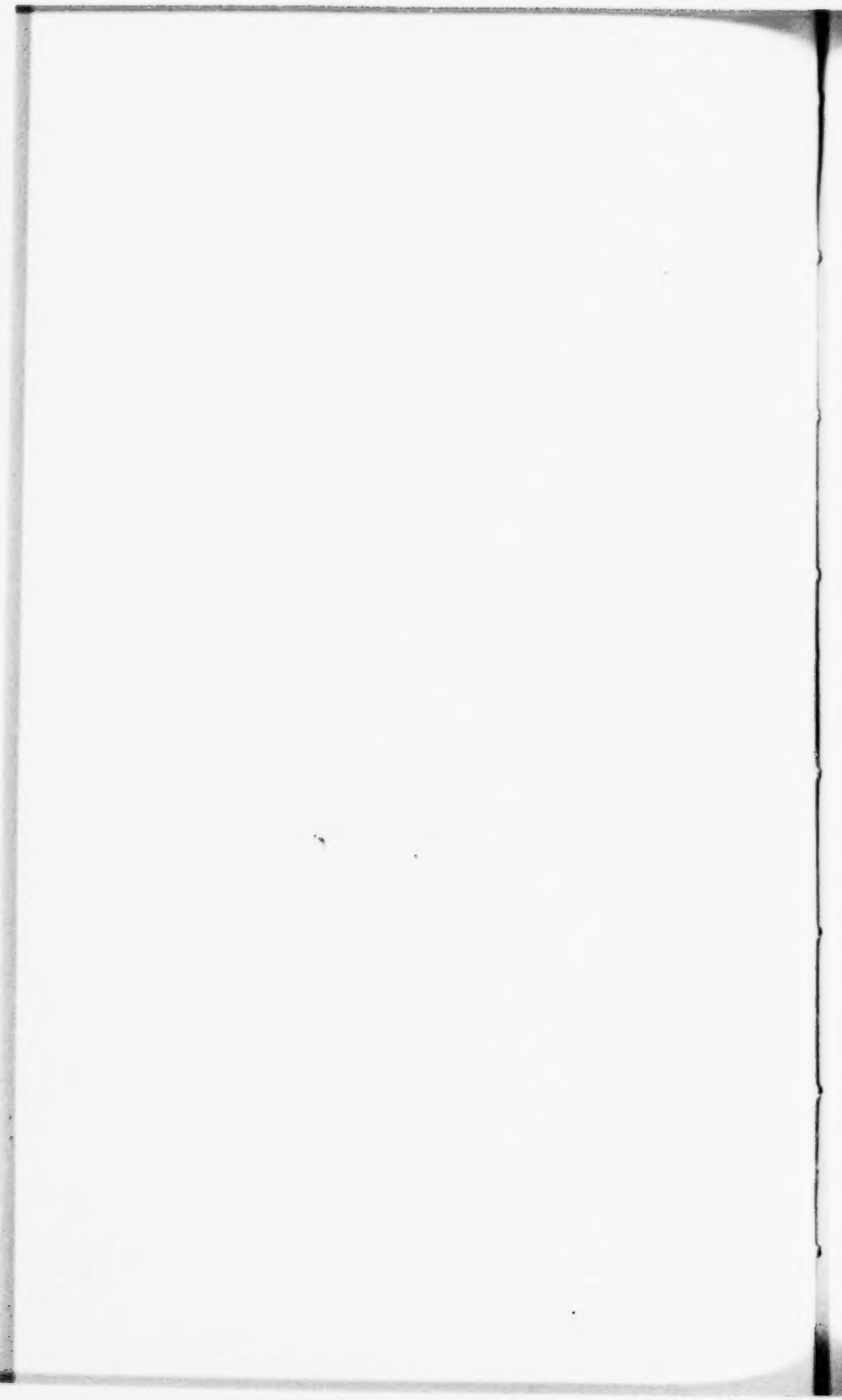
BRIEF

On Behalf of Petitioners

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INDEX

	Page
Table of Citations	ii
I. Opinions Below	1
II. Reports of Interstate Commerce Commission	3
III. Jurisdiction	4
IV. Question Presented	4
V. Statement	6
VI. Specification of Errors	22
VII. Summary of Argument	23
VIII. Argument	26
1. The Commission did not have power to approve or certify the so-called "forced merger" plan of reorganization	26
2. The 5% bondholders are debtor's equitable owners and in that capacity are entitled to vote under §5(11) of the Interstate Commerce Act on the question of corporate assent by debtor to the merger, consolidation or transfer	43
3. The "cram-down" provision in §77(e) of the Bankruptcy Act conferred no power on the Commission	50
4. The court's "cram-down" power does not authorize confirmation of the so-called "forced merger" plan of reorganization	52
5. The 1935 amendments to §77 do not authorize the "forced merger," because the inclusion in §77(e) of the Boyd case "fair and equitable" standard requires the retention of creditors' property rights as in equity receiverships and precludes their divestment by "forced merger"	63
Conclusion	71

OPY

Appendix A—Pertinent provisions of §77 of Bankruptcy Act, as enacted in 1933 and as revised in 1935, set out in parallel columns..... 73

Appendix B—Pertinent provisions of §5 of Interstate Commerce Act, as enacted by Transportation Act of 1920 and codified in 49 USCA §5, bound volume.... 84

Appendix C—Pertinent provisions of §5 of Interstate Commerce Act, as amended by Transportation Act of 1940 and codified in 49 USCA §5, pocket part supplement 86

TABLE OF CITATIONS

Cases

Atlantic Coast Line R Co v St Joe Paper Co, 179 F2d 538 (CA 5, 1950, cert den 339 US 929) 2, 6, 9, 10, 13, 17, 18, 35

Bondholders Committee v Commissioner, 315 US 189 (1942) 44

Boston Water-Power Co v Boston & W R Corp, 40 Mass 360 (1839).....60, 62

Callaway v Benton, 336 US 132 (1949)..... 43

Cary Library v Bliss, 151 Mass 364, 25 NE 92, 7 LRA 765 (1890) 60

Case v Los Angeles Lbr Products Co, 308 US 106 (1939) 63, 65, 67

Cleveland & P R Co, Petitioner, 2 Pittsb R 348 (Pa 1862) 62

Consolidated Rock Products Co v DuBois, 312 US 510 (1941) 64

Continental Illinois N B & T Co v Chicago R I & P R Co, 294 US 648 (1935).....39, 57, 63, 69

Ecker v Western P R Corp, 318 US 448 (1943).....39, 65

BLUR

BLEED THROUGH

Elkins Elec R Co v Western Maryland R Co, 163 F 724 (1908), aff 186 F 1022 (1911), cert den 223 US 725 (1911) 61

Fidelity Assurance Assn v Sims, 318 US 608 (1943)..63, 69
Florida East Coast Ry Co, In re, 52 F Supp 420 (DC Fla, 1943) 2, 14
Florida East Coast Ry Co, In re, 81 F Supp 926 (DC Fla, 1949) 2, 6, 9, 10, 13, 17, 21, 35, 36, 44, 45
Florida East Coast Ry Co, In re, 103 F Supp 825 (DC Fla, 1952) 2, 8, 9, 10, 11, 12, 13, 18
Florida East Coast Ry Co, In re, 201 F2d 325 (CA 5, 1953) 1, 2, 7, 10, 20, 36, 52
Florida East Coast Ry Co, In re, 201 F2d 332 (CA 5, 1953) 2
Florida East Coast Ry Co v Shaw, 11 F2d 653 (DC Fla, 1926) 60

Gibbons v Ogden, 9 Wheat 1 (1824)..... 59

Hanover Natl Bank v Moyses, 186 US 181 (1902)..... 57
Harbor Boom Co v Superior Ct Pac County, 65 Wash 129, 117 P 755 (1911)..... 62
Helvering v Alabama Asphaltic Limestone Co, 315 US 179 (1942) 44, 45, 66
Helvering v Cement Investors, Inc, 316 US 527 (1942) 44, 46
Helvering v New Haven & S L R Co, 121 F2d 985 (CA 2, 1941).....44, 47

Institutional Investors v Chicago M St P & P R Co, 318 US 523 (1943).....44, 64

Kneeland v American Loan & Trust Co of Boston, 136 US 89 (1890) 66

Lake Shore & M S Ry Co v Chicago & W I R Co, 97 Ill 506 (1881) 60, 61
Long Island Water Supply Co v Brooklyn, 166 US 685 (1897) 60

ED COPY

Louisville Joint Stock Land Bank v Radford, 295 US 555 (1935) 57, 58, 66

Marine Harbor Properties v Manufacturer's Trust Co, 317 US 78 (1942) 67

Northern Pacific R Co v Boyd, 228 US 482 (1913) 25, 45, 64, 65, 67, 71

Oregon Cascade R Co v Bailey, 3 Or 164 (1869) 62

Preble Corp v Wentworth, 84 F2d 73 (CA 1, 1936) .. 71

Railroad Retirement Board v Alton R Co, 295 US 330 (1935) 58

Reconstruction Finance Corp v Denver & R G W R Co, 328 US 495 (1946) 63, 65

Reiman, In re, DC NY, Fed Case No. 11,673 (1874) ... 57

Sabine & E T Ry Co v Gulf & I Ry Co, 92 Tex 162, 46 SW 784 (1898) 62

Samish Boom Co v Union Boom Co, 32 Wash 586, 73 P 670 (1903) 62

Schwabacher v United States, 334 US 182 (1948) . 29, 32, 39

Sharon Ry Appeal, 122 Pa St 533, 17 A 234 (1888) ... 62

St Joe Paper Co v Atlantic C L R Co, 345 US 948 ... 4

Thompson v Texas Mexican R Co, 328 US 134 (1946) . 27

United States v Bekins, 304 US 27 (1938) 57

United States v Chicago, M St P & P R Co, 282 US 311 (1931) 59

Utilities Power & L Corp, In re, 29 F Supp 763 (DC Ill, 1939) 66

Wilson v Atlantic C L R Co, 345 US 948 (1953) 4

West River Bridge v Dix, 6 How 507 (1848) 60, 61

Western Union Telegraph Co v Pennsylvania R Co, 195 US 540 (1904) 58

Wright v Union Central Life Ins Co, 304 US 502 (1938) 57, 58

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BLEED THROUGH

Texts

American Jurisprudence, Vol 18, Eminent Domain
§37 60
§97 60
§128 59
Collier on Bankruptcy (14th ed) Vol 6
p 3872, n 48 65
Corpus Juris Secundum, Vol 29, Eminent Domain
§191b 59
Lewis on Eminent Domain (3 ed) §§ 682, 756..... 59
Nichols on Eminent Domain (3 ed)
Vol 1, §2.2(8)..... 60
Vol 3, §8.2..... 59

Statutes

Act of March 3, 1933, 47 Stat 1474, c 204..... 30
Act of August 27, 1935, 49 Stat 911, c 774..... 30
Bankruptcy Act
§77 (11 USC §205) 19, 20, 22, 23, 25, 26, 27, 29, 30, 36, 38, 39, 41, 43, 44, 45, 47, 48, 50, 63, 65, 66, 67, 70
§77(a) (11 USC §205(a))..... 48
§77(b) (11 USC §205(b))..... 19, 22, 26, 30, 31, 40, 42, 50
§77(d) (11 USC §205(d))..... 30
§77(e) (11 USC §205(e))..23, 24, 25, 30, 31, 49, 50, 52, 53, 63, 64, 65, 66, 67, 69
§77(f) (11 USC §205(f))..... 17, 20, 23, 26, 27, 28, 31, 40
§77B (11 USC §207)..... 46
Chapter X 65, 69
Chapter XI 69
Chapter XII 69
Chapter XIII 69
28 USCA §1254(1) 4
Interstate Commerce Act §5 (49 USCA §5) 23, 24, 26, 29, 30, 31, 32, 43, 48, 49, 52, 53
Transportation Act of 1920 (41 Stat 456) 29
Transportation Act of 1940 (54 Stat 898) 30, 31

D COPY

United States Constitution
Art 1, §8, Clause 3 .....38, 58
Art 1, §8, Clause 4 38
Fifth Amendment 56, 57, 63

Federal Rules of Civil Procedure, Rule 71A 56
Senate Report No. 1395, 82d Congress, 2d Session, par 43 69
House Report No. 2320, 82d Congress, 2d Session, par 43 69
Historical Statistics of the United States, 1789-1945, published by the Department of Commerce, at page 320 65

Interstate Commerce Commission Reports

Consolidation of Railroads, 159 ICC 522 (1929)..... 29
Florida East Coast Ry Co Reorganization, 252 ICC 423 (1942) 3, 14
Florida East Coast Ry Co Reorganization, 252 ICC 731 (1942) 3, 14
Florida East Coast Ry Co Reorganization, 261 ICC 151 (1945) 3, 9, 14, 15, 34, 44
Florida East Coast Ry Co Reorganization, 267 ICC 295 (1947) 3, 9, 10, 12, 15, 16, 21, 27, 29, 34, 35
Florida East Coast Ry Co Reorganization, 267 ICC 729 (1948) 3, 9, 10, 15, 16, 17, 21, 28, 40, 43, 44, 50
Florida East Coast Ry Co Reorganization, 282 ICC 81 (1951) 3, 8, 9, 10, 13, 18, 19, 21, 35
Florida East Coast Ry Co Reorganization, 282 ICC 195 (1951) 4, 9, 10, 18, 19, 44

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BRIEF

On Behalf of Petitioners

I.

OPINIONS BELOW

The Court of Appeals opinions in connection with the judgment under review are reported as *In re Florida East Coast Ry Co,* 201 F2d 325 (CA 5, 1953). They are in Volume II of the record, at pages 717-733.[1]

1 This reference is to the record in No. 24 October Term, 1953. All subsequent references are to that record unless otherwise stated.

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Circuit Judge Strum's District Court opinion in connection with his order disapproving the Interstate Commerce Commission's fourth plan for the reorganization of debtor under §77 of the Bankruptcy Act, which order was reversed by the judgment under review, is reported as *In re Florida East Coast Ry Co,* 103 F Supp 825 (DC Fla, 1952). It is in Volume I of the record, at pages 127-168.

Judge Strum's opinion as District Judge disapproving the first plan of reorganization is reported as *In re Florida East Coast Ry Co,* 52 F Supp 420 (DC Fla, 1943). It is in Volume VI of the record, at pages 690-697.

Circuit Judge Sibley's District Court opinion disapproving the third plan of reorganization is reported as *In re Florida East Coast Ry Co,* 81 F Supp 926 (DC Fla, 1949). It is in Volume V of the record, at pages 466-481.

The Court of Appeals opinions in connection with its judgment affirming Judge Sibley's disapproval of the third plan are reported as *Atlantic Coast Line R Co v St Joe Paper Co,* 179 F2d 538 (CA 5, 1950). They are in Exhibit B attached to the petition for certiorari herein.

The Court of Appeals opinion in a separate appeal involving the allowance of liens to the extent of money deemed to have been advanced by the bondholders does not affect the question presented here. It is reported as *In re Florida East Coast Ry Co,* 201 F2d 332 (CA 5, 1953), but is not in the record.

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II.

REPORTS OF INTERSTATE COMMERCE COMMISSION

The report of April 6, 1942 approving the first plan of reorganization is reported as *Florida East Coast Ry Co Reorganization,* 252 ICC 423. It is in Volume VI of the record, at pages 528-640.

The Supplemental Report of August 10, 1942 modifying the first plan is reported as *Florida East Coast Ry Co Reorganization,* 252 ICC 731. It is in Volume VI of the record, at pages 641-689.

The Second Supplemental Report of January 8, 1945 approving the second plan is reported as *Florida East Coast Ry Co Reorganization,* 261 ICC 151. It is in Volume IV of the record, at pages 151-194.

Examiner Jewell's Proposed Third Supplemental Report is in Volume VI of the record, at pages 734-848.

The Third Supplemental Report of April 8, 1947 approving the third plan is reported as *Florida East Coast Ry Co Reorganization,* 267 ICC 295. It is in Volume IV of the record, at pages 295-391.

The Fourth Supplemental Report of March 25, 1948 adhering to the third plan is reported as *Florida East Coast Ry Co Reorganization,* 267 ICC 729. It is in Volume IV of the record, at pages 729-759.

The Fifth Supplemental Report of July 12, 1951 approving the fourth plan is reported as *Florida East Coast Ry Co Reorganization,* 282 ICC 81. It is in Volume I of the record, at pages 81-191.

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The Sixth Supplemental Report of October 25, 1951 adhering to the fourth plan is reported as *Florida East Coast Ry Co Reorganization*, 282 ICC 195. It is in Volume I of the record, at pages 195-226.

III.

JURISDICTION

Jurisdiction to review the judgment of the Court of Appeals by writ of certiorari is conferred on this Court by 28 USC §1254(1).

The judgment of the Court of Appeals was rendered January 19, 1953. (II, 734) Petitioners' petition for rehearing was denied March 2, 1953.[2] Their petition for writ of certiorari was filed in this Court April 10, 1953. It was granted May 4, 1953 limited to question I presented by the petition for writ of certiorari in No. 24 October Term, 1953. (345 US 948)

IV.

QUESTION PRESENTED

The following is the question to which the Court limited review in granting certiorari (345 US 948):

> "I. It being clear that Section 77 of the Bankruptcy Act, as enacted in 1933, did not authorize the Interstate Commerce Commission to present a plan of reorganization of a railroad involving a 'forced' merger of the debtor Railway with another railroad, the question is whether amendments to the 1933 Act, made in 1935, do authorize forced mergers.

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2 Exhibit A attached to the petition for certiorari herein.

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"The Act of 1933 for railroad reorganizations in bankruptcy contained in subdivision (b) a so called consistency clause which qualified the powers of the Commission in respect of mergers, by expressly providing that a merger would have to be brought about by compliance with '*provisions*' of the Interstate Commerce Act which allowed mergers *only* if requested and agreed to by the carrier and then approved by the Commission, after notice to the Governors of the states, and after hearing communities and shippers served by the carriers. This 'consistency' provision in this legislation was repeated in subd. (e) of the 1933 Act, where it was said that transfers of property or consolidations or mergers may be made 'to the extent contemplated by the plan *consistent with the purposes* of the Interstate Commerce Act as amended'. It will be noted that the clause in (b) used the word 'provisions' and the clause in (e) used the word 'purposes'. By amendments in 1935 these two 'consistency' clauses were consolidated and transplanted from (b) and (e) to subdivision (f).

"In the 1935 Act, subd. (f), the clause allowing transfer and mergers had the qualification 'to the extent contemplated by the plan' and 'not inconsistent with the provisions and purposes of Chapter 1 of Title 49 as on August 27, 1935 or thereafter amended.'

"The narrow question is therefore whether the mere transfer of the 'consistency' clauses from subdivisions (b) and (e) to subdivision (f) altered the meaning of the clauses and gave to the Interstate Commerce Commission a power to force mergers, which was withheld from it under the Act of 1933."

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V.

STATEMENT

The judgment under review was rendered by the United States Court of Appeals for the Fifth Circuit, two of five judges dissenting, in the appeal numbered and entitled on its docket 14163, *In the Matter of Florida East Coast Railway Company, Debtor—Atlantic Coast Line Railroad Company, Appellant, v St Joe Paper Company, et al, Appellees.* (II, 734)

The judgment reversed an order by Circuit Judge Strum, presiding in the United States District Court for the Southern District of Florida, Jacksonville Division.

Judge Strum's order disapproved the Interstate Commerce Commission's fourth plan for the reorganization of debtor under §77 of the Bankruptcy Act. (I, 168-170) Based on the disapproval and on a finding of "undue delay in a reasonably expeditious reorganization" of debtor, the order also dismissed the §77 proceeding and directed the return of debtor to a predecessor equity receivership, in order that the previously stayed foreclosure of the mortgage securing payment of debtors 5% bonds could be completed. (I, 169-170)

Judge Strum's grounds of disapproval were that the fourth plan, like the third, is "neither fair nor equitable" and "does not afford due recognition to the rights of the 5% bondholders, particularly the minority groups." (I, 168) He did not attempt to pass on the question of "forced merger" as such, since he believed that he was bound by "the law of the case" established in a prior appeal.[3] In that appeal disapproval of the third plan[4]

3 *Atlantic Coast Line R Co v St Joe Paper Co*, 179 F2d 538 (CA 5, 1950)

4 *In re Florida East Coast Ry Co*, 81 F Supp 926 (DC Fla, 1949)

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was affirmed, but two of three judges who sat in the Court of Appeals disagreed with Circuit Judge Sibley's District Court decision that §77 and the Interstate Commerce Act should be construed together and, so construed, they do not authorize a plan forcing debtor into a merger, consolidation or property transfer which an overwhelming majority in amount of its bondholder-equitable owners do not consent to but oppose strongly. (81 F Supp 926)

The prevailing opinion in connection with the judgment reversing Judge Strum also followed the same law of the case. The question now presented was decided principally by reiteration of the views of the two judges in the earlier appeal. The other material parts of the opinion are largely a series of dogmatic assertions that the findings of the commission majority are supported by evidence and Judge Strum's are not, and that the commission majority was right and Judge Strum was wrong. (201 F2d 325)

The minority opinion by Judge Russell, with whom Judge Borah joined, cited Judge Sibley's District Court disapproval of the third plan and agreed with him that §77 and the Interstate Commerce Act do not authorize a plan forcing debtor into a merger, consolidation or transfer which is not consented to but is opposed by a large majority in amount of its bondholder-equitable owners. (201 F2d 325)

The question grows out of the private, non-competitive, coerced sale which would result from the enforcement against debtor's equitable owners of the so-called "forced merger" provisions of the fourth plan. They are that in the event of respondent, Atlantic Coast Line Railroad Company, accepting the commission majority's offer of sale and giving its voluntary assent:

1. All of debtor's business, assets, franchises and property shall be "vested" in Coast Line free and clear of all

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of debtor's indebtedness and discharged from the lien of the 5% mortgage securing payment of $82,125,000 principal and defaulted interest coupons as of March 1, 1953.

2. The vesting shall be accomplished by merger of debtor into or its consolidation with or transfer and conveyance of its property to Coast Line.

3. The 5% bondholders shall be compelled to accept unwanted Coast Line securities having par and stated values totaling $42,500,000, together with an illusory $4,000,000 cash,[5] in extinguishment of their present equitable ownership of debtor. (282 ICC 213-226; I, 213-226)

The purport and effect of the "forced merger" provisions are that, subject to acceptance of the offer by Coast Line's equitable owners but without the consent and over the objections of debtor's equitable owners, a commission majority offered to sell debtor's property to Coast Line, free and clear of liens and debts, at a price debtor's equitable owners had no voice in fixing, which has never been determined to be the fair value of the property and is not payable in money, but represents only debtor's so-called "reorganization value" payable 91% in unacceptable Coast Line securities.

Even at this late date Coast Line is not bound. It is free to withdraw at any time. There is not and cannot be an enforceable contract between Coast Line and the commission majority.

The disapproved third plan provided for the same "forced merger," except that it would have extinguished

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[5] Judge Strum said: "*** A. C. L. puts in $4,000,000 in cash, and simultaneously receives from the estate of the debtor $4,000,000 in cash. This is a mere exchange of dollars, which benefits the present 5% bondholders not at all. The two amounts simply cancel." (103 F Supp 838)

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the 5% bondholders' equitable ownership of debtor by requiring them to accept unwanted Coast Line securities having par and stated values aggregating $36,375,000, together with $4,125,000 cash. (267 ICC 747-759; IV, 747-759)

The equitable ownership of debtor by the 5% bondholders results from the fact that when the trustees holding the mortgage securing payment of their bonds brought suit to foreclose it in 1932, and had receivers appointed, debtor was and has been at all times since and is now insolvent in the bankruptcy sense of liabilities exceeding assets. It was insolvent in that sense when the 5% bondholders brought the §77 proceeding in 1941. (81 F Supp 928; 103 F Supp 828) Beginning with the Commission's first report of April 6, 1942 and continuing throughout the six supplemental reports, debtor's capital stock was found to be without value and, therefore, to represent no equity or equitable ownership, and the 5% bondholders are the senior class of creditors whose securities will not be paid in full. (VI, 588, 632, 682; 261 ICC 172; IV, 172; 267 ICC 756; IV, 756; 282 ICC 224; I, 224)

Petitioners comprise one of the minority 5% bondholder groups referred to by Judge Strum. (81 F Supp 930; 179 F2d 540) St. Joe Paper Company, a petitioner in No. 24 October Term, 1953, and affiliated interests, own a majority of the bonds. (81 F Supp 930; 179 F2d 540; 103 F Supp 842) They frequently are referred to collectively as the majority bondholder.

The "forced merger" provisions of the third and fourth plans have been consistently opposed both before the Commission and in the courts on behalf of the holders of overwhelming majorities in amount of the 5% bonds. (267 ICC 295-391; IV, 295-391; 267 ICC 729-747; IV, 729-747; 282 ICC 81-191; I, 81-191; 282 ICC 195-212; I, 195-212)

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The third plan was objected to in the District Court and opposed in the Court of Appeals on behalf of the holders of more than 98% in amount. (81 F Supp 932; V, 476; 179 F2d 542; page 7 of Exhibit B attached to the petition for certiorari herein)

Objections to the fourth plan were interposed in the District Court on behalf of the holders of more than 99% in amount (103 F Supp 833; I, 138), and Coast Line's meager bondholder support disintegrated entirely before the case reached the Court of Appeals the second time. The fourth plan was not supported there, and is not supported here, by any bondholder. Coast Line was then, and is now, its only proponent.

Coast Line is one of debtor's three connecting carriers. It is not being reorganized under §77 or otherwise, is not and has never been affiliated with debtor in any way, and has never controlled or been controlled by debtor, nor has either ever had any proprietary interest in the other. The two railroads have never been commonly owned or controlled. There has never been any interlocking, overlapping or integration of their financial structures. They have always been completely independent of each other, their only relationships having been that of connecting carriers and joint owners of a steamship line from Miami to Cuba. (267 ICC 295-391; IV, 295-391; 267 ICC 729-747; IV 729-747; 81 F Supp 926; V, 466-481; 179 F2d 538; pages 1-22 of Exhibit B attached to the petition for certiorari herein; 282 ICC 81-191; I, 81-191; 282 ICC 195-212; I, 195-212; 103 F Supp 825; I, 127-168; 201 F2d 325; II, 717-733)

Debtor's capital structure is simple and uncomplicated. It is (103 F Supp 828):

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First Mortgage 4½% Bonds due January 1, 1959 ..... (Originally $12,000,000)	$ 8,189,000
First and Refunding Mortgage 5% Bonds due September 1, 1974	45,000,000
Capital Stock	37,500,000
Total	$90,689,000

During the pendency of the reorganization proceeding debtor's trustees have purchased from earnings and now hold $3,811,000 of the $12,000,000 first mortgage bonds. They and their predecessor receivers have paid from earnings all interest due on the bonds of that issue. The issue is not and has never been in default. They also have on hand accumulated earnings more than sufficient to retire the principal. (103 F Supp 828)

When Judge Strum disapproved the fourth plan they had paid from earnings $7,875,000 defaulted interest on the 5% bonds. (103 F Supp 828) They have since paid from earnings $4,500,000 additional defaulted interest. As of March 1, 1953 the interest coupons in default amounted to $37,125,000.

Debtor is the only double track railroad in Florida. It owns and operates 366 miles of modern rock ballasted main line double track on the east coast of Florida from Jacksonville, the second largest city in the state, to Miami, the largest. It is the most direct railroad connection between those cities. It also owns and operates single track branch lines which increase its total operated track to 571 miles. The branch lines extend to the truck-growing areas around Lake Okeechobee and those south of Miami. New Industries are constantly being located along its lines, one of

which alone will produce to debtor an annual revenue of $700,000. (103 F Supp, 842-843)

From Jacksonville south to the Palm Beaches, a distance of 299 miles, debtor has no rail competition and is the only rail carrier serving St. Augustine, Daytona Beach, New Smyrna Beach, Titusville, Cocoa, Melbourne, Vero Beach, Fort Pierce, Stuart and smaller communities. From the Palm Beaches south to Miami it serves Lake Worth, Boynton Beach, Delray Beach, Boca Raton, Deerfield Beach, Pompano Beach, Fort Lauderdale, Port Everglades, Dania, Hollywood and smaller communities, in competition with Seaboard Airline Railway. (103 F Supp 843)

Debtor's lines are fully protected by the most modern electrically operated safety system. They have recently been rerailed with new 112 and 115 pound steel rails at a cost of approximately $9,000,000, all paid out of earnings. Its rolling stock, purchased mainly from earnings, consists largely of Diesel locomotives, the latest and most modern streamlined passenger equipment and adequate modern freight equipment, with which it provides fast freight and local service and with its connecting carriers furnishes daily passenger service in high speed trains from New York, Chicago, Detroit and other points, via Jacksonville, to Miami and intermediate points. (103 F Supp. 843)

Coast Line, Seaboard and Southern Railway are debtor's connecting carriers at Jacksonville. They now compete for debtor's interchange business through the Jacksonville "open gateway." Debtor has no other connecting carrier. (103 F Supp 845)

Seaboard and Southern are petitioners in No. 24 October Term, 1953. Before the Commission and in the lower courts they vigorously objected to the proposed merger, consolidation or transfer. (267 ICC 336-339; IV, 336-339; 81

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F Supp 927; 179 F2d 539; 282 ICC 140-142; I, 140-142; 103 F Supp 827; 201 F2d 325)

Coast Line has a double track main line from Richmond to Jacksonville, and main lines from Jacksonville to Tampa, Birmingham and Atlanta, but has no line from Jacksonville to Miami. (179 F2d 541; 103 F Supp 844) Coast Line's basic purpose in submitting to the Commission offers to purchase debtor's property, and the basic purpose of the commission majorities in making counter-offers of sale, was to enable Coast Line to acquire at a bargain debtor's double track main line from Jacksonville to Miami. (81 F Supp 934; 179 F2d 542; 103 F Supp 844)

Coast Line's President made the following statement to its Board of Directors:

> "*** the rails of the Florida East Coast Railway represent a logical extension of this Company's lines into the lucrative East Coast section of Florida, not now directly served by this Company, and that he has for a number of years considered it was desirable that this Company should acquire that property or control thereof and operate same as a part of this Company's system *** the property operated as part of this Company, with consequent operating savings, should produce average annual net earnings available for fixed charges of about $1,700,000, which would be sufficient to meet reasonable fixed and contingent charges and *leave some residue of profit for this Company.* *** the advantages of being an 'originating' and 'terminating' line in Florida East Coast territory, which is perhaps the most highly developed section of the State of Florida, should produce for this Company *added earnings* on additional traffic which would be transported by this Company beyond the line of the present Florida East Coast Railway, that is, north

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of Jacksonville, although the amount of such adde earnings cannot be properly evaluated." (Emphasi supplied—St Joe Paper Co Exhibit X)

The Board immediately adopted a resolution authorizin the Chairman or the President to file such applications o petitions to the Commission or the court, and take suc other and further action in connection with the reorgani zation of debtor, as might be necessary to effect the pu chase by Coast Line of "Common Stock of the reorganize company."

During the pendency of the reorganization proceedin Coast Line purchased unsecured claims against debto aggregating $1,900,000 which the Commission had found t be without value. It paid $5,000 for the claims and agree with the former owners to pay an additional 50% of wha ever might be realized on them, less expenses. Until bought the unsecured claims, Coast Line never had an financial interest in debtor, and was not even a creditor (VI, 920-921; IV, 144-146)

Coast Line's initial appearance in the proceeding cam after Judge Strum had disapproved the Commission first plan[6] and hearings before the Commission on a secon plan had been closed. The appearance took the form a petition to have the proceeding reopened for the sub mission of a plan under which Coast Line would acquir control of the reorganized debtor by a forced sale to Coa Line of 60% of the new common stock. (261 ICC 187-19 IV, 187-193)

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6 The plan provided that the 4½% first mortgage bondholders shou receive new first mortgage bonds equal in amount and seniority to t bonds then held, and the 5% bondholders should receive, for each $1,0 bond, $100 of new general mortgage bonds and 10 shares of no par val stock. (252 ICC 423; VI, 528; 252 ICC 731; VI, 641) It was disapprov solely on the ground that it should have allocated for reorganization pu poses, instead of leaving as a floating surplus, accumulated earnin amounting to approximately $17,000,000. (52 F Supp 420; VI, 690-697)

The Commission unanimously rejected this proposal[7] and approved a second plan providing for the 4½% first mortgage bonds to be paid in full from accumulated earnings, the setting aside of $8,700,000 from accumulated earnings as reserves for betterments and improvements and cash requirements upon reorganization, and the receipt by the 5% bondholders, for each $1,000 bond, of $450 new first mortgage income bonds and 4½ shares of new common stock. (261 ICC 170-187; IV, 170-187)

On petitions for modification the Commission reopened the proceeding and Coast Line proposed the "forced merger." (267 ICC 295-298; IV, 295-298) The proposal was a unilateral offer by Coast Line to purchase debtor's property. The offer was submitted to the Commission for acceptance. It was not made to the debtor, its trustees or equitable owners, and did not have their concurrence or consent. It was not binding on Coast Line. (267 ICC 300; IV, 300)

After lengthy hearings, the Examiner's full and carefully considered report recommended strongly that the second plan be modified in relatively minor respects and otherwise be adhered to. (VI, 734-848)

By a five to four vote,[8] the Commission overruled the Examiner and approved Coast Line's "forced merger"

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7 For the reasons, among others, that the securities proposed, taken at par, would fall far short of satisfying the amount of the claim of the 5% bondholders and if, in their view, the prospects of future earnings or the control value were such that the stock might later have a market value in excess of par and they desired to hold it to realize the higher price, they should be at liberty to do so, as they would not be reimbursed in full on their claim by accepting $100 per share for stock representing a part of their share of debtor's estate; the majority bondholder would vote to reject the proposal; the $77 power to order a judicial sale of the property of debtor for the benefit of creditors did not confer power "to sell the interests of one or all the creditors to another creditor or to an outsider for the benefit of the purchaser"; and the proposal was prima facie impracticable. (261 ICC 187-193; IV, 187-193)

8 In Commissioner Mahaffie's first dissent (267 ICC 390; IV, 390), in which four other Commissioners joined, some initially, others later (267 ICC 747; IV, 747), he said: "Aside from what seems to me a fatal legal

proposal, with modifications, as the Commission's third plan. (267 ICC 390-391; IV, 390-391) By this approval the majority made a counter-offer to sell debtor's property to Coast Line at a price slightly higher than the one Coast Line had offered to pay. Coast Line could not accept the counter-offer without first amending its charter to authorize the issuance of the class of preferred stock provided for.[9] Coast Line's stockholders avidly adopted a resolution accepting the counter-offer and assenting to the acquisition of debtor's property.[10]

The report making the counter-offer refused to permit a judicial sale of the property. The reason given was that it would defeat the proposed transfer, "since Coast Line obviously could not compete successfully in bidding with the debtor's first and refunding bondholders." (267 ICC 307; IV, 307)

Upon reconsideration by the full Commission the counter-offer was adhered to by a six to five vote. (267 ICC 729-747; IV, 729-747) The report adhering to it stated that the offering price did not "represent worth of the property such as would be determined by an inventory of the physical assets," nor "physical value," nor "market

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defect in the report, I think it wrong on the merits. *** I would approve a plan which, in its main features, is substantially as proposed by the examiner. This would permit the property to be reorganized. The result of the present report, in my judgment, is more likely to be prolonged litigation." (267 ICC 391; IV, 391)

9 "RESOLVED, that in order to effect the acquisition of the properties of Florida East Coast Railway Company and to issue the class of preferred stock specified by the Interstate Commerce Commission in its Report and Order dated March 25th, 1948, this Board of Directors of this Company now recommends to the stockholders that the Charter of this Company as now existing be amended ***." (III, St Joe Paper Co Exhibit X, resolution adopted by Coast Line's Board of Directors)

10 "RESOLVED, that the Stockholders of Atlantic Coast Line Railroad Company in meeting assembled do hereby accept the Plan of reorganization of Florida East Coast Railway Company, as approved by the Interstate Commerce Commission in its Reports and Orders, dated April 8th, 1947, and March 25th, 1948, in the pending Florida East Coast Railway Company reorganization proceeding, and hereby assent to the acquisition of the properties of that Company by Atlantic Coast Line Railroad Company as provided in said Plan ***." (III, St Joe Paper Co Exhibit X)

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lue," but represented only debtor's "Value for reorgan-ation purposes" payable in Coast Line securities. (267 C 736; IV, 736)

The plan was disapproved by Circuit Judge Sibley pre-ding in the District Court. (81 F Supp 926; V, 466). His ounds were that §77 and the Interstate Commerce Act, nstrued together, did not authorize a plan forcing debtor to a merger, consolidation or transfer to which the 5% ondholders by an overwhelming majority do not con-nt" (81 F Supp 932; V, 476), but if it did, and was thin constitutional bankruptcy power, the plan was not ir and equitable and did not afford due recognition to e rights of the bondholders.

The Court of Appeals affirmed, one of three judges dis-nting. (179 F2d 538; pages 1-22 of Exhibit B attached to e petition for certiorari herein)

This Court denied Coast Line's petition for certiorari. 39 US 929) However, two judges in the Court of Ap-eals concluded that Judge Sibley was wrong on the ques-on of "forced merger." Chief Judge Hutcheson said, nd the effect of Judge Holmes' dissenting opinion was to gree, "that a plan providing for what the trial judge roadly called a 'forced merger', that is, a merger over e objection of the debtor and all its creditors, might be wfully certified to the court and lawfully approved and nfirmed by it." (179 F2d 544)

So far as can be ascertained from their respective pinions, neither appellate judge gave any consideration o the effect of the "consistency" clause in §77(f), con-erring on the Commission limited power, "upon confirma-ion of a plan," to "grant authority for the *** transfer f any property, sale, consolidation or merger of the ebtor's property *** to the extent contemplated by the lan *and not inconsistent with the provisions and pur-*

poses of the Interstate Commerce Act as now or hereafter amended." (Emphasis supplied)

Judge Russell concurred in Chief Judge Hutcheson's opinion only to the extent that it affirmed Judge Sibley's order, but said he was in "complete accord" with Judge Sibley's conclusions and could not accept contrary views expressed by Chief Judge Hutcheson. (179 F2d 545) Thus he agreed with Judge Sibley's decision that §77 and the Interstate Commerce Act do not authorize a plan forcing debtor into a merger, consolidation or transfer which an overwhelming majority in amount of its bondholder-equitable owners do not consent to but oppose.

The views of Judges Hutcheson and Holmes on the question of "forced merger" have been regarded by the Commission and the courts as the law of the case in all subsequent proceedings.

Coast Line proposed another "forced merger." (282 ICC 87; I, 87) This proposal, too, was a unilateral offer to purchase debtor's property at a price claimed to be better than the one fixed by the commission majority in the disapproved third plan. The new offer, like the first, was submitted to the Commission for acceptance. It was not made to the debtor, its trustees or equitable owners. It did not have their concurrence or consent. Like the first offer, it was not binding on Coast Line.

With modifications, Coast Line's new "forced merger" proposal was approved by a seven to three vote as the Commission's fourth plan. (282 ICC 81-191; I, 81-191) By this approval the commission majority made another counter-offer to sell debtor's property to Coast Line, asserting that the new price was better than the one fixed in the earlier counter-offer.[11] Coast Line's stockholders adopted

11 Judge Strum found: "*** the bondholders are receiving, for the property itself, $1,340,000 less under the fourth plan than under the third." (103 F Supp 840)

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a resolution accepting the new offer and assenting to the acquisition of debtor's property.[12]

Unlike the report making the earlier counter-offer, the report making the new one says nothing about a judicial sale, but it does not provide for one. (282 ICC 81; I, 81; 282 ICC 213; I, 213) It does say that the new offering price represents "the value of the debtor's property in terms of Coast Line securities, including one-half of the prospective savings." (282 ICC 160; I, 160)

Petitions for modification submitted by these petitioners and others were denied by a seven to three vote. (282 ICC 195-212; I, 195-212)

Judge Strum disapproved the plan as unfair, inequitable, and not a due recognition of the rights of the 5% bondholders. (I, 168-170)

Much of the prevailing opinion reversing Judge Strum is devoted to an exposition of the areas of agreement and disagreement between Judges Hutcheson and Holmes in the prior appeal. The opinion then says: "Turning, for the correct answer to this question, to the record as it now stands before us, we are not in any doubt that, under the plain terms of subsection (b)(5) of Sec. 77 of the Act, 11 U.S.C.A.§205, which provides that the plan 'may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations *** ' the commission was precisely authorized to formulate and recommend a plan providing, as the fourth plan does,

12 "RESOLVED, that the Stockholders of Atlantic Coast Line Railroad Company in meeting assembled do hereby accept the Plan of Reorganization of Florida East Coast Railway Company, as approved by the Interstate Commerce Commission in its Reports and Orders, dated July 12th, 1951, and October 25th, 1951, in the pending Florida East Coast Railway Company re-organization proceeding, and hereby assent to the acquisition of the properties of that Company by Atlantic Coast Line Railroad Company as provided in said Plan ***."

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for the merger of East Coast and Coast Line." (201 F2d 329)

This opinion, too, fails to disclose that any consideration was given to the limitation of power imposed on the Commission by the "consistency" clause in §77(f).

Judge Borah joined in Judge Russell's dissenting opinion. It points out that "The bald proposition established by the majority opinion is that the court's power in bankruptcy authorizes the taking, against the wishes of the overwhelming majority of the refunding bondholders, of their existing rights, requiring acceptance by them of an entirely different and unrelated security which they do not desire." It says that "This holding poses a serious constitutional question as to whether the court's power in bankruptcy could thus be extended to force a merger consistent with the Fifth Amendment." (201 F2d 331)

The dissent goes on to say: "*** I do not reach the constitutional question because here it is clear from the history of the legislation of Section 77, that the Commission has undertaken to exercise a power which the Congress never intended to confer on the Commission. This was well pointed out by Judge Sibley in his decision while sitting as District Judge in a former proceeding in this matter. *** This view was expressly approved by the writer in his special concurrence upon the former appeal of this case. *** It is reaffirmed today." (201 F2d 331-332)

Petitioners submitted the only petition for rehearing. It was denied. Judges Russell and Borah dissented. (Exhibit A attached to the petition for certiorari herein)

A truly remarkable aspect of the case is that every presiding officer who heard evidence disapproved the pro-

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posed forced merger, and all decisions approving it were by commissioners or judges who had neither seen nor heard any witness and were not as well qualified to evaluate the evidence.

Examiner Jewell heard evidence in Washington, D. C., November 6-9, 1945 and in West Palm Beach, Florida, November 13-30, 1945. (VI, 735-736) He recommended that the Commission disapprove the proposed forced merger. (VI, 797-798) Judge Sibley heard evidence in Jacksonville, Florida, January 10-13, 1949. (IV, 118; V, 461) He disapproved the third plan. (81 F Supp 926) Judge Strum heard evidence in Jacksonville, Florida, February 4-7, 1952. (II, 247, 659) He disapproved the fourth plan. (103 F Supp 825)

No evidence was heard by the five Commissioners who overruled Examiner Jewell and made the first counter-offer of sale (267 ICC 297; IV, 297), nor was any heard by the six Commissioners who adhered to the report overruling him (267 ICC 729; IV, 729), nor by the seven Commissioners who made the second counter-offer of sale (282 ICC 81; I, 81), nor by any judge who sat in the Court of Appeals.

VI.

SPECIFICATION OF ERRORS

The Court of Appeals erred in the following respects:

1. In deciding that §77 of the Bankruptcy Act authorizes the so-called "forced merger" plan of reorganization.

2. In deciding that §77(b) of the Bankruptcy Act confers on the Interstate Commerce Commission power to approve and certify a plan of reorganization providing, without the assent and over the objections of an overwhelming majority in amount of debtor's equitable owners, for a merger, consolidation or transfer resulting from the Commission's having entertained and considered respondent's unilateral offer to purchase debtor's property, and the acceptance by respondent of a commission majority counter-offer to sell it.

3. In reversing Judge Strum's order disapproving the so-called "forced merger" fourth plan of reorganization.

4. In directing Judge Strum to approve the so-called "forced merger" fourth plan of reorganization.

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VII.

SUMMARY OF ARGUMENT

1. The Commission did not have power to approve or certify the so-called "forced merger" plan of reorganization. The consistency clause in §77(f) of the Bankruptcy Act requires the construction in pari materia of the merger, consolidation and transfer provisions of §5 of the Interstate Commerce Act and §77(b) of the Bankruptcy Act. Review of the integrated provisions of §77 and §5 establishes that Congress intended and required that all mergers, consolidations and transfers should be carrier-initiated and voluntary.

The combined consistency clause in §77(f) of the 1935 Act, like its two predecessors in §77(b) and (e) of the 1933 Act, requires consistency with both the "provisions and purposes" of the Interstate Commerce Act. The fact that the combined clause is framed in the form of a limitation on the powers exercisable by the Commission after confirmation does not govern its application. The Commission must determine that a merger, consolidation or transfer will be "consistent" before it can approve or certify a plan, otherwise the certified plan will be lacking in permissible means of execution.

2. The 5% bondholders are debtor's equitable owners and in that capacity are entitled to vote under §5(11) of the Interstate Commerce Act on the question of corporate assent by debtor to the merger, consolidation or transfer. If debtor's capital stock represented value and equitable ownership, the stockholders would be entitled to vote under §5(11) on the question of corporate assent. The 5% bondholders are in fact the equitable owners. They stepped into the shoes of the stockholders, and in those shoes succeeded to the right to vote. To say that the right is con-

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trolled by the technicality of stock-ownership, as against bond-ownership, rather than by equitable ownership would sacrifice substance to form.

3. The "cram-down" provision in §77(e) of the Bankruptcy Act conferred no power on the Commission. It gave the court, but not the Commission, a new power.

4. The court's "cram-down" power does not authorize confirmation of the so-called "forced merger" plan of reorganization. It does not apply to the first vote—the group vote of equitable owners on the question of corporate assent to the merger, consolidation or transfer, to be taken under §5(11) of the Interstate Commerce Act. The power applies solely to the second vote in connection with a plan providing for a merger, consolidation or transfer. This is the individual vote of each affected creditor or equitable owner, to be taken under §77(e) of the Bankruptcy Act, on the question of acceptance or rejection of a plan approved by Commission and court. The factors and considerations involved in this vote have long been within the equity and bankruptcy jurisdiction of courts—fair and equitable treatment, due recognition of rights, unfair discrimination, conformity to requirements of law of land, and reasonable justification for rejective action.

The cram-down provision does not confer power on the court to determine or decide what is best for owners in regard to keeping or selling property they have chosen and lawfully own, it being a fundamental concept of our system of government that what a man chooses to own, if lawful, cannot be taken away from him in consideration of something that a court thinks is as good or better, except under the power of eminent domain.

The purpose of the cram-down provision is to prevent dissident minorities, in the sense of minority classes of inferior claims in a complicated financial structure, a

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situation which does not exist here, from blocking confirmation of a plan approved by Commission and court—to obviate the exacting of inequitable adjustments by obstructive minorities as the price of their consents.

Because Congress intended constitutional application of the cram-down provision, it should not be given the unconstitutional application proposed by the commission and court of appeals majorities.

5. The 1935 amendments to §77 do not authorize the "forced merger," because the inclusion in §77(e) of the *Boyd* case "fair and equitable" standard requires the retention of creditors' property rights as in equity receiverships and precludes their divestment by "forced merger."

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VIII.

ARGUMENT

1. The Commission Did Not Have Power to Approve or Certify the So-Called "Forced Merger" Plan of Reorganization.

The provisions of §77 of the Bankruptcy Act[13] expressly integrate §77 with the Interstate Commerce Act, thus requiring that they be construed in pari materia to ascertain and give effect to the intent of Congress.

The consistency clause in §77(f) requires that a merger, consolidation or property transfer provided for in a plan of reorganization shall be consistent with the "provisions and purposes" of the Interstate Commerce Act. Thus, it requires the construction in pari materia of the merger, consolidation and transfer provisions of §5 of the Interstate Commerce Act and §77(b) of the Bankruptcy Act.

So construed, the manifest intent and explicit provisions are that the consistency clause limits the Commission's §77(b) merger, consolidation and transfer powers to those conferred by the Interstate Commerce Act, and precludes the approval or certification by the Commission of a plan of reorganization providing for a merger, consolidation or transfer which has not been consented to by the requisite majority of a debtor's equitable owners.

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13 The material parts of statutes referred to are set out in appendices.

Appendix A sets out in parallel columns the pertinent parts of §77 of the Bankruptcy Act, as enacted originally in 1933 and as revised in 1935, in order that the changes in their provisions may be noted.

Appendix B sets out the pertinent parts of §5 of the Interstate Commerce Act, as enacted by the Transportation Act of 1920 and codified in 49 USCA §5.

Appendix C sets out the pertinent parts of §5 of the Interstate Commerce Act, as amended by the Transportation Act of 1940 and codified in 49 USCA §5, pocket part supplement.

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The integration of the two Acts is demonstrated in *Thompson v Texas Mexican R Co,* 328 US 134, 144 (1946), which says:

> "The commission has further functions to perform apart from determining under §77 whether it would be consistent with the reorganization requirements of the debtor to terminate the trackage agreement.
>
> "By §1(18) of the Interstate Commerce Act, 49 USCA §1(18) 10A FCA title 49, §1(18), it is provided that 'no carrier by railroad subject to this chapter shall abandon all or any portion of a line of railroad, or the operation thereof, unless and until there shall first have been obtained from the commission a certificate that the present or future public convenience and necessity permit of such abandonment.' *Carriers being reorganized under §77 of the Bankruptcy Act are not exempt from that provision.*" (Emphasis supplied)

It would be strange indeed if Congress had intended that a debtor in a §77 reorganization proceeding could not be authorized to abandon a trackage agreement except in compliance with the Interstate Commerce Act, but could be deprived of all property by forced merger, consolidation or transfer without regard to its provisions.

The integration of the two Acts was not noticed or discussed in any of the prevailing opinions in the Court of Appeals. The consistency clause in §77(f) was not mentioned or referred to. Nothing was said regarding its effect. So far as those opinions are concerned it does not exist.

It was discussed by the commission majorities. In the third supplemental report the majority said (267 ICC 308; IV, 308):

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"The Coast Line plan, by which control would be transferred to that carrier, is in effect a request or application to us by one carrier for authority to acquire control of another and, in conformity with the provisions of subsection (f) of section 77 of the Bankruptcy Act that the transfer of the properties of a debtor be not inconsistent with the provisions and purposes of the Interstate Commerce Act, the record should contain the information required in a proceeding under section 5(2) of the Interstate Commerce Act."

In contrast, the majority said in the fourth supplemental report that the consistency clause in §77(f) "is not a limitation on the plan which we are authorized to approve under subsection (b)." (267 ICC 731)

The effect of that statement, as applied, was to assert that Coast Line could submit to the Commission a unilateral offer to acquire debtor's property, and the Commission could accept it or make a counter-offer for acceptance or rejection by Coast Line, all without the concurrence or consent of the debtor, its trustees or equitable owners.

To the contrary, review of the integrated provisions of the controlling statutes establishes that Congress intended and required that all mergers, consolidations and transfers should be carrier-initiated and voluntary. The requirements are that every merger, consolidation or transfer, whether involving solvent railroads or debtor railroads in §77 proceedings, or both, must be the voluntary result of arm's length bargaining between or among them, and be assented to by the requisite majorities of the equitable owners of each railroad involved. Until 1940 it also was required that every merger, consolidation or transfer be in harmony with and in furtherance of the nation-wide

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plan of consolidations adopted in compliance with the Transportation Act of 1920. The Commission's statutory power is that, with the assent of each railroad involved, and upon proper application, notice and hearing, it can approve and authorize a voluntary merger, consolidation or transfer, but it has never been given the power to coerce one.

As enacted by the Transportation Act of 1920,[14] §5 of the Interstate Commerce Act directed the Commission to "prepare and adopt" a nation-wide plan for the consolidation of railroads into "a limited number of systems."[15] It gave the Commission power to approve and authorize consolidations "if all the carriers involved assent thereto,"[16] and if "in harmony with and in furtherance of" the nation-wide plan of consolidations.[17] It did not confer power to compel them.[18] The purpose of these provisions was to permit and encourage railroad-initiated voluntary consolidations assented to by "all the carriers involved," conforming to the nation-wide plan.[19]

In the nation-wide plan adopted in 1929[20] debtor was allocated to the Southern Railway System. (267 ICC 343; IV, 343) Thus, even a carrier-initiated voluntary agreement, assented to by both railroads, for the merger or consolidation of debtor with or the transfer of its property to Coast Line would have violated the nation-wide plan when §77 of the Bankruptcy Act was enacted in 1933, and when it was revised in 1935, and until the Transportation

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14 Act of February 28, 1920, 41 Stat 456, c 91, 49 USCA §5

15 §407(4), 49 USCA §5(4)

16 §407(6)(c), 49 USCA §5(6)(c)

17 §407(6)(a), 49 USCA §5(6)(a)

18 *Schwabacher v United States*, 334 US 182 (1948)

19 Case cited in footnote 18

20 Consolidation of Railroads, 159 ICC 522

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Act of 1940[21] released the Commission from adherence to the nation-wide plan.

When §77 was enacted in 1933,[22] and when it was revised in 1935,[23] §5 of the Interstate Commerce Act was not changed. As enacted originally, §77 required that any plan of reorganization recommended by the Commission to the interested parties (§77(d)) should provide adequate means for its execution. (§77(b)) The means could include a merger, consolidation or transfer "so far" as would be "consistent with the provisions of §§ 1 and 5 of the Interstate Commerce Act as amended." (§77(b))

This could mean only a merger, consolidation or transfer to which "all the carriers involved assent" and in "harmony with and in furtherance of" the nation-wide plan. It limited the merger, consolidation and transfer powers of the Commission to those conferred by §5 of the Interstate Commerce Act. It limited the Commission to the previously conferred power of approval and authorization, and did not confer a new power to compel.

That this was the meaning is borne out by the subsequent provision that, following acceptance of a plan by the affected creditors and stockholders, the Commission could approve it and grant authority to effectuate any merger, consolidation or transfer provided for "consistent with the *purposes* of the Interstate Commerce Act as amended" (§77(e)—emphasis supplied), one of which was to encourage the railroad consolidations authorized by §5.

When §77 was revised in 1935, §5 of the Interstate Commerce Act was not changed. It continued to provide that

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21 Act of September 18, 1940, 54 Stat 898, c 722, 49 USCA §5(2)

22 Act of March 3, 1933, 47 Stat 1474, c 204

23 Act of August 27, 1935, 49 Stat 911, c 774

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the Commission could approve and authorize a consolidation only "if all the carriers involved assent thereto" and if in conformity with the nation-wide plan.

The two consistency clauses in §77(b) and (e) of the 1933 Act were combined and transferred to §77(f) in the 1935 revision. The combined clause is that "Upon confirmation of a plan the Commission shall, without further proceedings, grant authority for the * * * transfer of any property, sale, consolidation or merger of the debtor's property *** to the extent contemplated by the plan and *not inconsistent with the provisions and purposes of the Interstate Commerce Act as now or hereafter amended.*" (Emphasis supplied)

The 1935 revision requires that a commission approved plan provide adequate means for its execution. (§77(b)) The means may include a merger, consolidation or transfer (§77(b)), but the Commission cannot grant authority to effectuate a merger, consolidation or transfer "inconsistent with the provisions and purposes of the Interstate Commerce Act." (§77(f)) Necessarily, a merger, consolidation or transfer which the Commission cannot grant authority to effectuate cannot be the means for the execution of a plan.

Section 5 of the Interstate Commerce Act was amended by the Transportation Act of 1940,[24] but the combined consistency clause in §77(f) of the Bankruptcy Act was not changed. It continues to require that a merger, consolidation or transfer provided for in a plan of reorganization shall not be "inconsistent with the provisions and purposes of the Interstate Commerce Act as now or hereafter amended."

"The Transportation Act of 1940 relieved the Commission of formulating a nation-wide plan of consolidations.

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24 Act of September 18, 1940, 54 Stat 898, c 722, 49 USCA §5

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Instead, it authorized approval by the Commission of carrier-initiated, voluntary plans of merger or consolidation ***." [25]

Under §5(2)(a) of the Interstate Commerce Act, as amended by the Transportation Act of 1940, the Commission may approve and authorize a voluntary merger or consolidation of two or more railroads, or one railroad's voluntary sale of its property to another. Approval of a voluntary merger, consolidation or transfer "within the scope of the Act is dependent upon three, and upon only three, considerations: First, a finding that it 'will be consistent with the public interest.' (§5(2)(b)) Second, a finding that, subject to any modification made by the Commission, it is 'just and reasonable.' (§5(2)(b)) Third, assent of a 'majority, unless a different vote is required under applicable State law, in which case the number so required shall assent, of the votes of the holders of the shares entitled to vote.' (§5(11))" [26]

Reading all of these provisions together, they make it crystal clear that the Commission does not have the power to approve or certify a plan of reorganization providing, without the consent and over the objection of a debtor's equitable owners, for a merger, consolidation or transfer resulting from the Commission's having entertained and considered another railroad's unilateral offer to acquire the debtor's property, and the acceptance by the other railroad of a commission majority counter-offer to dispose of it.

The statutory provisions limit the Commission's merger, consolidation and transfer powers to approval and authorization of voluntary mergers, consolidations and transfers resulting from arm's length bargaining between the

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25 *Schwabacher v United States*, 334 US 182, 193 (1948)

26 *Schwabacher v United States*, 334 US 182, 194 (1948)

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railroads involved. This was provided not only because it is the historic American approach to the process of purchase and sale, but also because it is the only means by which the equitable owers of each railroad can be reasonably assured that they will not be deprived, even by honest mistake, of any value to which they may be entitled.

It is the only method by which the equitable owners of each railroad can claim and enforce their right to be paid the values which they believe to be inherent in their property. It is the only way in which equitable owners, as investors, can preserve intact their right to be paid or have the benefit of future earnings, and to determine when, how and for what consideration they will dispose of that right.

There was no arm's length bargaining here. The sale price fixed by the commission majority in its last counter-offer does not represent a price negotiated by owners willing but not compelled to sell and a buyer desirous but not compelled to purchase.

Debtor's equitable owners had no voice in fixing the price for which the commission majority says their property must be sold. All they have been able to do is to clamor that the Commission has no power to sell it, but nevertheless is offering it for sale at an unconscionably low price. And if the Court of Appeals majority is right, there can be no judicial review of the question whether the commission majority's offering price is unconscionably low.

Inherent in all that was done is the undeniable fact that the commission majority could not adopt an owner's bargaining approach, nor could it exercise an owner's bargaining latitude. An owner can set his price and lower or

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increase it as he sees fit, or as may become necessary or advisable because of his necessities, financial difficulties, prosperity or other changing circumstances. He can make an offer and tell the prospective buyer to "take it or leave it." Normally he is not under compulsion to fix a price which he believes will prove attractive to a prospective purchaser.

The commission majority was under that compulsion. It had to set a price which it thought would prove attractive to Coast Line. To set one which it thought would not prove attractive—one which it thought Coast Line would not accept—would have been futile. To be certain of not setting a price higher than Coast Line would be willing to pay, the majority had to subordinate the rights of debtor's equitable owners to the primary objective of making it possible for Coast Line to purchase debtor's double track main line from Jacksonville to Miami. All other things—rights, values, equities, purchase price and terms of payment—had to be secondary and subordinate to that objective.

That the commission majority, in order to be assured of effecting a sale to Coast Line, was compelled to and did sacrifice the rights, values and equities of debtor's equitable owners to the fixing of a price and terms of payment which it thought would prove attractive to Coast Line, is demonstrated by the developments in this case.

Coast Line first made the Commission an offer to buy 60% of the reorganized debtor's common stock. (261 ICC 187; IV, 187) The Commission unanimously rejected the offer. (261 ICC 190-193; IV, 190-193)

Coast Line then made the Commission an offer to purchase debtor's property. (267 ICC 296; IV, 296) The Commission found expressly that the offer "is inequitable in that it does not provide for full satisfaction of the value

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the claims of the debtor's creditors." (267 ICC 389, par 5; IV, 389, par 15)

A commission majority made a counter-offer. (267 ICC 72; IV, 372) Coast Line accepted. (III, St Joe Paper to Exhibit X)

Presumably the majority thought its counter-offer was equitable, but Judge Sibley found that it was not fair and equitable and did not afford due recognization to the rights of the 5% bondholders. (81 F Supp 926) The Court of Appeals affirmed. (179 F2d 538) This Court denied certiorari. (339 US 929)

Judge Sibley said: "The very aggressiveness of the Coast Line in proposing and defending this plan indicates that the Coast Line thinks it is getting a bargain; that what it gets is not the mere equivalent of what it pays, but much more." (81 F Supp 934) Chief Judge Hutcheson added: "The case we have here is that of one railroad company coveting, and pressing to possess, a competing debtor railroad company, against the wishes of 98 percent of the equitable owners of the debtor ***." (179 F2d 542)

Following the final disapproval of the third plan, Coast Line made another offer to the Commission. (282 ICC 87; I, 87) The Commission found that the new offer "would not fully compensate the debtor's creditors for surrendering their property rights." (282 ICC 163; I, 163)

A commission majority made another counter-offer. (282 ICC 181; I, 181) Coast Line accepted. (III, ACL Exhibit 10)

Presumably the majority thought the second counter-offer was equitable, but Judge Strum found that, like the first counter-offer, it is "neither fair nor equitable" and "does not afford due recognition to the rights of the 5%

bondholders, particularly the minority groups." (I, 168-170) Three of the five judges who sat in the Court of Appeals differed with him, and thought the commission majority had set a sufficient price. (201 F2d 325)

The controlling statutes do not contemplate any such dickerings between Coast Line and the commission majorities, with debtor's equitable owners excluded from any voice in fixing the price at which the commission majority offered to sell their property.

Judge Sibley's views, in which Judges Russell and Borah emphatically concurred, are cogent and compelling. They were that the Interstate Commerce Act is to be construed with §77 to ascertain the intent of Congress and, so construed, they authorize the Commission to approve bilateral agreements for mergers or consolidations of railroads or transfers of their property, but do not confer authority for the Commission to enter into negotiations with Coast Line for the sale of debtor's property, Judge Sibley said (81 F Supp 932-933):

> "It is very earnestly argued that Subsection b which gives the specifications for a plan, in saying it 'may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation,' etc., does not mean a forced merger, which the Interstate Commerce Act, 49 U. S. C. A. §1 et seq., has never permitted the Commission to compel, though Congress has often considered the matter. The history of the legislation in adopting Section 77 in 1933, is pointed to as showing that Congress was then concerned that no such thing was to be done under Section 77; and so again in 1935 when the section was revised; and that the reference to the Interstate Commerce Act in Subsection f which the Commission

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thinks applies only to its actions after confirmation of a plan, was intended to apply throughout and became accidentally misplaced in redrafting the Act. Without reciting the history, I think this contention is true. *** this question *** relates to the extent of the power granted by Congress to its own agent. And the Interstate Commerce Act can be construed with Section 77 to ascertain what Congress really meant by a railroad 'merger or consolidation', and whether it means one consented to by both parties to it. No one would contend that the Coast Line could be forced. But the Commission argues that this debtor has also consented, because its stockholders have not appeared to object. I think that does not follow. It is expressly found that the debtor's insolvency is such that the stockholders are not interested parties. The debtor, its property and affairs now belong in equity to the creditors, and more specifically to the refunding bondholders. The full jurisdiction and control over them is in this court. The refunding bondholders by an overwhelming majority do not consent. If the court has the power as a court of bankruptcy to consent for them, under the circumstances of this case it should refuse to do so. I do not think Congress intended to force a merger undesired by the majority in amount of the affected parties by permitting a merger to be part of a plan. ***

"This railroad property is in equity the property of the refunding bondholders who replace practically the stockholders as owners. On a reorganization they would naturally receive the common stock pro rata. All the plans approved by the Commission save the present one so provided. With that set-up it would not much matter what reorganization value and total capitalization was fixed; for the common stockholders would get the surplus earnings. ***

> "This case is not as though the merging corporations were affiliates, and members of the same corporate family already. In such a case there is really a mere simplification of corporate organization of interests already related. The Coast Line, though an unsecured creditor, is really a stranger in interest, having been found to have no interest in the railroad property to be reorganized."

Petitioners are informed that the legislative history referred to by Judge Sibley will be reviewed in other briefs. For that reason it is not reviewed here.

Petitioners' position is that the legislative history clearly and explicitly sustains and confirms the conclusion that the consistency clause limits the Commission's merger, consolidation and transfer powers to those conferred by the Interstate Commerce Act.

The basic reason for the limitation is that the power of Congress to provide for the relief and rehabilitation of financially distressed railroads flows from the bankruptcy power,[27] while the commerce power[28] is the source of the power to regulate mergers, consolidations and transfers, and the latter had been the subject matter of much controversy and legislation prior to the enactment of §77 in 1933.

Reading §77 as written, the unmistakable purpose and intent was to extend the "subject of bankruptcies" into a field not then occupied, by providing for the relief and rehabilitation of financially distressed railroads, but to preserve intact the existing national policy regulating mergers, consolidations and transfers.

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27 Constitution, Article 1, §8, Clause 4: "The Congress shall have Power *** To establish *** uniform Laws on the subject of Bankruptcies throughout the United States ***."

28 Constitution, Article 1, §8, Clause 3: "The Congress shall have Power *** To regulate Commerce *** among the several States ***."

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"Obviously, §77 does no more than follow the line of historical and progressive development projected by previous acts"; its scope and purpose is "an adjustment of a failing debtor's obligations."[29] It is "bottomed upon the theory of debtor rehabilitation by adjustment of creditors' claims."[30] It was not designed as legislation empowering the Commission to receive or accept a stranger railroad's gratuitous offer to acquire the property of a debtor, or to make a counter-offer for acceptance or rejection.

There was good reason for this. Acting under the commerce power, and after fullest discussion and consideration through the years, Congress had formulated and matured the national policy regulating mergers, consolidations and transfers. The policy and the provisions to effectuate it were expressed in the Interstate Commerce Act. The Commission had for many years sought power to compel mergers, consolidations and transfers, but Congress had consistently refused to grant it. This history is reviewed fully in *Schwabacher v United States,* 334 US 182 (1948). It will not be repeated here.

Suffice it to say that in enacting §77 Congress demanded and received unqualified assurances that it would not enlarge the merger, consolidation or transfer powers of the Commission, and took every precaution to make certain that it did not. This it accomplished by expressly limiting the powers to those conferred by the Interstate Commerce Act.

It certainly cannot be thought that by the enactment of §77 in 1933, or by its revision in 1935, Congress intended to empower the Commission, through the processes of bankruptcy, to approve or authorize a merger, consolidation or transfer contrary to the Interstate Commerce Act. The

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29 *Continental Ill N B & T Co v Chicago R I & P R Co,* 294 US 648, 673 (1935)

30 *Ecker v Western P R Corp,* 318 US 448, 469 (1943)

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consistency clause evidences the contrary intent—that any merger, consolidation or transfer provided for in a plan should be controlled by the "provisions" requiring that it be in harmony with and in furtherance of the nation-wide plan. That intent being obvious, there is no reason to think that Congress intended to require compliance with only that provision and to dispense with compliance with the one requiring the assent of "all the carriers involved."

The word "provisions" as used in the consistency clause is broad and all inclusive. There is nothing to indicate that Congress meant only one provision and not the other. The natural and logical conclusion is that Congress meant that a plan of reorganization could include only a merger, consolidation or transfer complying with the provisions requiring harmony with the nation-wide plan and assent by "all the carriers involved."

The combined consistency clause in §77(f) of the 1935 revision, like its two predecessors, requires consistency with both the "provisions and purposes" of the Interstate Commerce Act. Those provisions and purposes continue to encourage voluntary mergers, consolidations and transfers, and to permit their approval and authorization, but have never been enlarged to authorize compulsion.

The attitude of the commission majorities was that because the combined clause was transferred to §77(f), instead of being placed in §77(b) or elsewhere, it applies only to action by the Commission after confirmation of a plan, and no longer prohibits commission approval and certification of a plan providing for a merger, consolidation or transfer which is inconsistent with both the provisions and purposes of the Interstate Commerce Act. (267 ICC 731; IV, 731)

This attitude leads inevitably to one of two inadmissible results—either that because of its transfer to §77(f) the

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combined consistency clause is meaningless, is to be read out of §77, and is to be given no effect, or that the Commission can approve and certify to the court a plan providing for a merger, consolidation or transfer which is inconsistent with the provisions and purposes of the Interstate Commerce Act, and the court can approve and confirm it, but the Commission then cannot grant authority to effectuate it.

It is unthinkable that the combined consistency clause can properly be read out of §77, and be given no effect. In the first place, if that had been the intent, Congress would not have gone to the trouble of combining its two predecessor clauses and including them in their combined form in the 1935 revision. Instead, it would have omitted both, and the 1935 revision would have been silent on the subject of consistency.

In the second place, when §77 was revised, the established national regulatory policy, which was not changed until five years later, was that the railroads of the nation be consolidated into the limited number of systems provided for in the nation-wide plan, and that this should be accomplished by voluntary consolidations assented to by all the carriers involved and in harmony with and in furtherance of the master plan. If the intent had been that the national policy should not apply to railroads in reorganization, and that a merger, consolidation or transfer involving a debtor and another railroad could conflict with the nation-wide plan, or that one in harmony with the nation-wide plan could be forced by the Commission without the "assent" of the debtor, Congress would have said so plainly. That meaning cannot be attributed to the combined consistency clause.

The other alternative—that the Commission can entertain, approve and certify to the court a plan providing

for a merger, consolidation or transfer which is inconsistent with the provisions and purposes of the Interstate Commerce Act, and the court can approve and confirm it, but the Commission then cannot grant authority to effectuate it—is equally inadmissible. The mere statement of the proposition refutes it. Congress should not be subjected to the accusation of having intended to authorize the Commission and court to labor in vain to produce, approve and confirm a plan which cannot be carried into effect.

The plain meaning of the combined consistency clause, regardless of its location in the 1935 revision, is that it is just as much a limitation on the merger, consolidation and transfer provisions in §77(b) as if it had been placed in that section. The fact that it is expressed in the form of a limitation on the powers exercisable by the Commission after confirmation does not govern its application. The application is that a merger, consolidation or transfer inconsistent with the provisions and purposes of the Interstate Commerce Act cannot be the "means for the execution" of a plan.

What the Commission cannot do after confirmation, it cannot do at any earlier stage of the proceeding. The Commission cannot approve or certify that which it cannot grant authority to effectuate.

A merger, consolidation or transfer may be included in a plan only as a means of execution. The Commission must determine that a merger, consolidation or transfer will be "consistent" before it can approve or certify a plan, otherwise the certified plan will be lacking in permissible means of execution.

Indeed, the obvious purpose in framing the combined consistency clause in the form of a limitation on the authority that the Commission can grant, is to make it a limi-

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tation on all other provisions in §77—to make it plain that the Commission cannot, from the outset to the conclusion of the proceeding, take any action, or exercise any power, or entertain or consider any proposal, or approve or authorize any merger, consolidation or transfer, which is inconsistent with the provisions and purposes of the Interstate Commerce Act.

The combined consistency clause is a limitation which applies from the inception to the end of the proceeding. It limits the merger, consolidation and transfer powers of the Commission to those conferred by the Interstate Commerce Act, and those alone. In this case it prohibited the Commission from entertaining, as a complete plan of reorganization, Coast Line's unilateral offer to purchase debtor's property. It prohibited the approval and certification, as a plan of reorganization, of the commission majority's counter-offer to sell the property to Coast Line.

2. The 5% Bondholders Are Debtor's Equitable Owners and in That Capacity Are Entitled to Vote Under §5(11) of the Interstate Commerce Act on the Question of Corporate Assent by Debtor to the Merger, Consolidation or Transfer.

The commission majority argued: "The solvent corporation here is willing. There is nothing in the Interstate Commerce Act to prohibit us from approving such a transaction. *** There is nothing of record to show that the merger of the Florida East Coast with the Atlantic Coast Line is objected to by either. The stockholders of the Florida East Coast have not objected. The objection comes from certain of its bondholders." [31]

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31 Fourth Supplemental Report, 267 ICC 732; IV, 732. Cf., *Callaway v Benton*, 336 US 132, 138, footnote 6: "*** when the rights of bondholders of the lessor may be affected, as was the case with Terre Haute bondholders in the Milwaukee Railroad reorganization (see Group of

This overlooks the fact that debtor's "property is in equity the property" of the bondholders referred to, "who replaced practically the stockholders as owners." (81 F Supp 933) "It is expressly found that the debtor's insolvency is such that the stockholders are not interested parties. The debtor, its property and affairs now belong in equity to the creditors, and more specifically to the refunding bondholders." (81 F Supp 932) Because debtor's capital stock is without value and represents no equity or equitable ownership, and the 5% refunding bondholders are the senior class of creditors whose securities will not be paid in full, they are the equitable owners of debtor and its property. (VI, 588, 632, 682; 261 ICC 172; IV, 172; 267 ICC 756; IV, 756; 282 ICC 224; I, 224)

They became the equitable owners in 1932 when the trustees holding the mortgage securing payment of their bonds brought suit to foreclose it and had receivers of debtor appointed, or at the latest in 1941 when they instituted the proceeding for the reorganization of debtor under §77 of the Bankruptcy Act. (81 F Supp 928; 103 F Supp 828) They were as much the owners when their trustees brought the foreclosure suit and secured the receivership as if a decree of foreclosure had been entered and the property had been sold to them; the decree and the sale would have done nothing but recognize officially what had before been true in fact.[32]

Institutional Investors v Chicago M St P & P R Co, 318 US 523, 87 L ed 959, 63 S Ct 727, 52 Am Bankr NS 526, and discussion infra), nearly unanimous consent of such bondholders may be required before the changes can be made effective. The Interstate Commerce Commission took that position in the Milwaukee case and provided that the offer to Terre Haute should not be deemed accepted unless substantially all of its bondholders voted to accept. Chicago M St P & P R Co Reorganization, 239 Inters Com (F) 485, 536-538; 240 Inters Com (F) 257, 270, 271. See also 318 US at 532, 533, 87 L ed 989, 990, 63 S Ct 727, 52 Am Bankr NS 526."

32 *Helvering v Alabama Asphaltic Limestone Co*, 315 US 179, 183 (1942); *Bondholders Committee v Commissioner*, 315 US 189 (1942); *Helvering v Cement Investors, Inc*, 316 US 527, 532 (1942); *Helvering v New Haven & S L R Co*, 121 F2d 985, 987 (CA2, 1941)

They were as much the owners when they initiated the §77 proceeding as if debtor had been reorganized in what Judge Sibley called "the simple and natural manner several times certified by the Commission unanimously by giving all the refunding bondholders a pro rata share of its common stock" (81 F Supp 929); the receipt of the common stock pro rata would have done nothing but recognize officially what had before been true in fact.[33]

Helvering v Alabama Asphaltic Limestone Co, 315 US 179 (1942), dealt with the question whether creditors became equitable owners of a bankrupt's property when they instituted an involuntary bankruptcy proceeding to effectuate a plan of reorganization by a bankruptcy sale of the property to a new corporation, whose stock would be issued to the creditors in satisfaction of their claims, thus invoking and enforcing the full priority rule of the Boyd case[34] and excluding the bankrupt's stockholders from participation. The Court said (315 US 183):

> "Technically that did not occur in this proceeding until the judicial sale took place. For practical purposes, however, it took place not later than the time when the creditors took steps to enforce their demands against their insolvent debtor. In this case, that was the date of the institution of bankruptcy proceedings. From that time on they had effective command over the disposition of the property. The full priority rule of Northern P. R. Co. v. Boyd, 228 US 482, 57 L ed 931, 33 S Ct 554, applies to proceedings in bankruptcy as well as to equity receiverships. Case v. Los Angeles Lumber Products Co. 308 US 106, 84 L ed 110, 60 S Ct 1, 41 Am Bankr Rep (NS) 110. It gives creditors, whether secured or unsecured, the right to exclude stockholders entirely from the reorganization

33 Cases cited footnote 32

34 *Northern P R Co v Boyd*, 228 US 482 (1913)

plan when the debtor is insolvent. See Re 620 Church Street Bldg. Corp. 299 US 24, 81 L ed 16, 57 S Ct 88, 32 Am Bankr Rep (NS) 185. When the equity owners are excluded and the old creditors become the stockholders of the new corporation, it conforms to realities to date their equity ownership from the time when they invoked the processes of the law to enforce their rights of full priority. At that time they stepped into the shoes of the old stockholders. The sale 'did nothing but recognize officially what had before been true in fact.' Helvering v. New Haven & S. L. R. Co. (CCA 2d) 121 F (2d) 985, 987."

In *Helvering v Cement Investors, Inc,* 316 US 527 (1942), the court considered the question whether owners of first mortgage bonds became equitable owners of the mortgaged property when the company filed a §77B petition under which a reorganization was effected by transfer of the property to a new company, which issued income bonds and common stock in exchange for the old bonds, but gave the stockholders of the debtor no interest in the new company except that in exchange for the stock they received warrants for the purchase of new shares. In deciding that question the court said (316 US 532):

"In case of reorganizations of insolvent corporations the creditors have the right to exclude the stockholders entirely from the reorganization plan. When the stockholders are excluded and the creditors of the old company become the stockholders of the new, 'it conforms to realities to date their equity ownership' from the time when the processes of the law were invoked 'to enforce their rights of full priority.' Helvering v. Alabama Asphaltic Limestone Co. 315 US 179, ante, 775, 62 S Ct 540. Under that approach the ownership of the equity in these debtor companies effectively passed to these creditors at least when §77B proceedings were instituted."

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The opinion in *Helvering v New Haven S L R Co,* 121 F2d 985 (CA 2, 1941) was by Judge Learned Hand. The controlling point was whether bondholders became equitable owners of mortgaged property on the date their trustee filed a state court bill to foreclose the mortgage securing payment of the bonds, and a reorganization was effected by foreclosure sale of the property to a bondholders committee, followed by the committee's transfer of the property to a new company in consideration of the issuance of the new company's common stock to the old bondholders. Speaking for the court, Judge Hand said (121 F2d 987):

> "Debts are payable in money and give creditors neither power to control the debtor's property, nor any concern with its vicissitudes while the debtor remains solvent; they do not share in his gains, or suffer from his losses. *** This ceases, however, as soon as the debtor becomes irrecoverably insolvent and the debts are due; the creditors are then entitled to control the property, and thereafter its adventures are their own. The debtor loses any rightful power to dispose of it except for an adequate price, and courts like to speak of him as a 'trustee'; all that is necessary to make them complete legal owners is that they shall follow the prescribed legal formalities. *** the bondholders were as much the owners before foreclosure as after; the decree and the sale did nothing but recognize officially what had before been true in fact."

Thus, in the instant case, the 5% bondholders "stepped into the shoes" of debtor's stockholders either in 1932, when their trustees brought the foreclosure suit and secured the receivership, or in 1941, when they instituted the §77 proceeding. They have at all times since one or the other of those events been in the shoes of debtor's stockholders.

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In those shoes, and in the exercise of the rights acquired by stepping into them, they are entitled to vote under §5(11) of the Interstate Commerce Act on the question of corporate assent by debtor to the proposed merger, consolidation or transfer. The proposed merger, consolidation or transfer cannot be forced or effectuated without "the assent *** of a majority, unless a different vote is required under applicable State law, in which case the number so required shall assent, of the votes of the holders of the" 5% bonds. (§5(11))

This can be illustrated by assuming that the 5% bondholders instituted the §77 proceeding because of insolvency not in the bankruptcy sense of liabilities exceeding assets, but in the equity sense of debtor being "unable to meet its debts as they mature." (§77(a)) That would mean either that the value of assets in excess of liabilities would impart value to debtor's capital stock, or that the value of the assets would at least equal liabilities and value would attach to the capital stock upon debtor becoming able to meet its debts as they mature.

In either event, the fact that the stock represented value and equitable ownership would mean that the stockholders would continue to have rights, one of which would be the right to vote on the question of merger, consolidation or transfer. No one would contend in this situation that the mere pendency of a §77 proceeding would invest the Commission with power to approve or certify a plan of reorganization providing, without the assent and over the objections of the stockholders, for a merger, consolidation or transfer resulting from the Commission's having entertained and considered another railroad's offer to acquire debtor's property, and the acceptance by the other railroad of a Commission counter-offer to dispose of it. No one would be so bold as to urge that the assent of the stockholders would not be required under §5(11) of the Interstate Commerce Act.

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Two separate votes, at different times, on different questions, and in different capacities, would be required. The first, to be taken before the Commission could approve or certify the plan, would be the group vote of stockholders at a regular or special meeting, under §5(11) of the Interstate Commerce Act, on the question of corporate assent to the merger, consolidation or transfer. The second, to be taken after approval and certification of the plan by the Commission and its approval by the court, would be the individual action of each affected creditor and stockholder, under §77(e) of the Bankruptcy Act, on the question of acceptance or rejection of the plan.

The vote of the stockholders at such a meeting would be their group or collective vote, in the capacity of stockholders, on the question of authorizing or not authorizing corporate action. It would be a part of the corporate mechanics by which the corporate assent to a merger, consolidation or transfer agreement would be given or withheld. It would have nothing to do with acceptance or rejection of the plan of reorganization.

Acceptance or rejection of the plan by each creditor and stockholder would be his individual act in the capacity of a person affected. The acceptance or rejection would not be given at any stockholders or other meeting, regular or special, and would not be a group or collective vote. The individual acceptances or rejections would not authorize or refuse to authorize any corporate action. They would have nothing whatever to do with corporate action. They would neither give nor withhold corporate assent to any merger, consolidation or transfer agreement.

The vote of the stockholders at a regular or special meeting would be required because they would be debtor's equitable owners. Here, the 5% bondholders are in fact the equitable owners. To say that the right to vote on the question of merger, consolidation or transfer is con-

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trolled by the technicality of stock-ownership, as against bond-ownership, rather than by equitable ownership, would sacrifice substance to form.

3. The "Cram-Down" Provision in §77(e) of the Bankruptcy Act Conferred No Power on the Commission.

The commission majority relied on the so-called "cram-down" provision in §77(e). It argued: "Any contention that the merger must be voluntary is nullified by the 1935 amendment to section 77, which provides, in subsection (e) that 'if the plan has not been accepted by the creditors and stockholders, the judge may, nevertheless, confirm the plan over their objection.' This provision is not restricted to any one of the several plans authorized in subsection (b). It refers to any plan authorized by that subsection. Subsection (b) specifically authorizes a plan which may provide for the merger of the debtor corporation with another corporation. Any involuntary aspects of such merger fade completely in the face of the power of the court to confirm the plan providing for such merger over the objection of creditors or stockholders."[35]

A patent fallacy in this argument is that the cram-down provision relates solely to the powers and functions of the court. It gave the court, but not the Commission, a new power. It did not give the Commission power to approve or certify a plan of reorganization providing for a merger, consolidation or transfer "inconsistent with the provisions and purposes of the Interstate Commerce Act." It did not give the Commission power to approve or certify a plan providing for a merger, consolidation or transfer to which debtor's equitable owners do not assent but object.

The reasoning of the commission majority involved this thought process: (1) After a plan certified by the Com-

35 Fourth Supplemental Report, 267 ICC 732; IV, 732

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mission has been approved by the court and rejected by some classes of interested parties, the court may nevertheless confirm it under specified circumstances and conditions; (2) therefore, before the Commission certifies a plan, it may approve one providing for a merger, consolidation or transfer which would be unauthorized if the court did not have the power of confirmation notwithstanding rejection; (3) therefore, the conferring on the court of power to confirm notwithstanding rejection released the Commission from the congressional mandate that it can approve and authorize only carrier-initiated, voluntary mergers, consolidations and transfers which are assented to by the equitable owners of each railroad involved; (4) therefore, the Commission can approve and certify a plan providing, without the consent and over the objections of debtor's equitable owners, for a merger, consolidation or transfer resulting from the Commission's having entertained another railroad's offer to purchase debtor's property, and the acceptance by the other railroad of a Commission counter-offer to sell it; (5) therefore, the Commission can approve and certify an unauthorized plan on the assumption that, notwithstanding the objections of debtor's equitable owners, the court can and will cram it down their throats.

The short answer is that the cram-down provision conferred no power whatever on the Commission.

It did not enlarge, reduce or affect the powers of the Commission.

It authorized no commission action.

It did not repeal or modify the requirement that if a merger, consolidation or transfer is to be the means for the execution of a plan, the merger, consolidation or transfer must be consistent with the "provisions and purposes" of the Interstate Commerce Act.

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4. The Court's "Cram-down" Power Does Not Authorize Confirmation of the So-called "Forced Merger" Plan of Reorganization.

In an attempt to fortify its previous dogmatic statements, and far in advance of the event, the prevailing opinion in the Court of Appeals holds that after the anticipated rejecting vote of the 5% bondholders, the "forced merger" plan must be confirmed unless "conditions should so change" as to render it no longer "fair and reasonable." (201 F2d 330-331) Thus, by a gratuitous and completely erroneous construction of the cram-down provision in §77(e), and without noticing or referring to the combined consistency clause, the court of appeals majority adopted and approved the contention of the commission majority that it could approve and certify a plan providing for a merger, consolidation or transfer violating both the provisions and purposes of §5 of the Interstate Commerce Act, and the court could and would cram it down the 5% bondholders' throats.

Since the Commission did not have power to approve or certify to the court the so-called "forced merger" plan, it was never properly before the court. Consequently, although Judge Strum disapproved it on other grounds, the disapproval was right, and the Court of Appeals was wrong in reversing and directing that it be approved. The Commission's lack of power to approve and certify the plan vitiates everything done subsequently.

A plan cannot be submitted to a debtor's affected creditors and equitable owners, for acceptance or rejection, until after the Commission has properly approved and certified it to the court, and the court has approved it. The so-called "forced merger" plan has never achieved that status, and can never do so. Therefore, it can never be submitted to debtor's affected creditors and equitable

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owners, for acceptance or rejection, and the jurisdiction of the court to decide whether it should be confirmed notwithstanding rejection can never be invoked or exercised.

Aside from the foregoing, the court's "cram-down" power applies solely to the second vote to be taken in connection with a plan providing for a merger, consolidation or transfer—the individual vote of each affected creditor or equitable owner, to be taken under §77(e) of the Bankruptcy Act, on the question of acceptance or rejection of a plan which has been properly approved and certified by the Commission and approved by the court. It does not apply to the first vote to be taken on such a plan—the group vote of equitable owners at a regular or special meeting, on the question of corporate assent to the merger, consolidation or transfer, to be taken under §5(11) of the Interstate Commerce Act, before the Commission can approve or certify the plan.

The two votes are on wholly different questions. They are by persons acting in completely different capacities. The factors and considerations governing them are entirely unrelated.

The second vote, which is not taken at any meeting, calls for individual acceptance or rejection of the plan by each affected creditor and equitable owner. The Commission takes this vote by submitting the plan, together with its reports or summaries and the opinion and order of the judge, to each affected creditor and equitable owner. (§77(e)) The question decided by the sum of their individual acceptances or rejections involves factors and considerations which have long been within the equity and bankruptcy jurisdictions of courts—fair and equitable treatment, due recognition of rights of classes of creditors and stockholders, unfair discrimination in favor of classes of creditors or stockholders, conformity to the require-

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ments of the law of the land regarding the participation of the various classes of creditors and stockholders, and reasonable justification for rejective action in the light of all the relevant facts and the respective rights and interests of those rejecting.

The first vote, the vote on the question of corporate assent to the merger, consolidation or transfer, is not by creditors and equitable owners, but is limited to equitable owners alone. It is not taken by submitting a question to each equitable owner individually, but is a group or collective vote at a regular or special meeting of the equitable owners. It does not relate to acceptance or rejection of the plan. Instead, it relates to the authorization or non-authorization of corporate action. It involves factors and considerations which have always been in the realm of business judgment and decision, and not within the equity, bankruptcy or other jurisdiction of courts—corporate assent to a merger, consolidation or transfer agreement voluntarily negotiated through the process of arm's length bargaining by a seller or sellers willing but not compelled to deal or sell, and a purchaser or purchasers desirous but not compelled to deal or buy.

These separate procedures, at the different times, are required by the combined consistency clause. Its overall effect is that if a plan provides a merger, consolidation or transfer as its means of execution, the means must be authorized by appropriate corporate action independent of acceptance or rejection of the plan by those whom it will affect.

This was ignored by the commission and court of appeals majorities. They seek to short-circuit the requirement of corporate authorization by treating the "means" as the "end," and assert that without corporate authorization or assent, a merger, consolidation or transfer can be

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crammed down the throats of equitable owners. The reason for their beclouded vision is that in this instance the proposed merger, consolidation or transfer is not utilized as the means for the execution of an otherwise fair and equitable plan, but was conceived, proposed and approved as the sole and only purpose, objective and end of the plan.

They propose to accomplish the short-circuiting under the cram-down provision, but lose sight of the fact that it does not apply to the vote on the question of corporate authorization of assent to a merger, consolidation or transfer. It is not the function of courts, nor within their jurisdiction, to determine or decide what is best for owners in regard to keeping or selling property they have chosen and lawfully own. A fundamental concept of our system of government is that what a man chooses to own, if lawful, cannot be taken away from him in consideration of something that a court thinks is as good or better, except under the power of eminent domain.

The cram-down provision authorizes confirmation of an unreasonably rejected plan which has been approved by both Commission and court. It does not authorize the court to cram down the throats of equitable owners a proposed merger, consolidation or transfer which they, in the exercise of their business judgment, have concluded and decided is unsatisfactory and objectionable to them, and to which they do not assent or agree.

The purpose of the cram-down provision is to prevent dissident minorities from blocking confirmation of a plan approved by Commission and court—to obviate the exacting of inequitable adjustments by obstructive minorities as the price of their consents. Because the acceptance of the holders of two-thirds in amount of the claims of any class binds the remainder of the class, and becomes the acceptance of the entire class, the dissident

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or obstructive minorities obviously cannot be and are not minorities within a class. Instead, they are minorities in the sense of inferior classes in a complicated financial structure. That situation does not exist here.

The commission and court of appeals majorities propose that the cram-down clause be used against debtor's equitable owners, although they are not an inferior, but are the senior and only interested class. The use proposed is to cram down their throats, not a plan which provides for rehabilitating debtor by scaling down indebtedness to bring it within ability to pay and issuing to the senior class of creditors new securities of the same enterprise in exchange for those now held, but one which provides for a merger, consolidation or transfer that is unsatisfactory and objectionable to them, as debtor's equitable owners, and to which, in the exercise of their business judgment, they do not assent or agree.

This would extend the scope of the bankruptcy power into the field of eminent domain, contrary to the inhibitions of the Fifth Amendment. To so use the cram-down provision would permit the taking of the bondholders' property by Coast Line—as much so and with identically the same effect as if Coast Line had proceeded directly under Rule 71A of the Federal Rules of Civil Procedure, by bringing an action in the district court to condemn debtor's property, had such a proceeding been possible.

The only differences would be that in the condemnation action Coast Line would be required (1) to pay compensation equal to the fair value of the property and, (2) to pay the compensation in money; but the cramming down of the proposed merger, consolidation or transfer would permit Coast Line (1) to pay only debtor's so-called "reorganization value" and, (2) to deliver its securities in payment of 91% of that value. This would be contrary to all concepts of due process and just compensation.

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By whatever name it is called, and whatever may be the excuse for it, the end result of the "forced merger" would be to take from the 5% bondholders their private property and vest it in Coast Line, forcing them to accept compensation payable 91% in unwanted Coast Line securities. The bankruptcy power of Congress does not empower that taking, nor is it authorized by the power of Congress to regulate interstate commerce.

The bankruptcy power is not susceptible of final definition, its scope being the "subject of the relations between an insolvent or nonpaying or fraudulent debtor, and his creditors, extending to his or their relief."[36] Nevertheless, "The bankruptcy power, like all the other great substantive powers of Congress, is subject to the Fifth Amendment."[37] That amendment prohibits the taking of private property for other than public use, and for public use permits a taking only by "due process of law" and upon payment of "just compensation."

As reviewed in the cited cases, the history and development of the Bankruptcy Act disclose that its original purpose was to effect ratable distribution among creditors of the property of an insolvent, non-paying or fraudulent debtor. It was later extended to relieve the honest debtor from oppressive indebtedness and permit him to start afresh. It has not been, it could not be, extended to primarily benefit a covetous purchaser of the insolvent estate. If that could be done, Congress could authorize initiation of a bankruptcy proceeding by a stranger seeking to acquire the property of an insolvent debtor, and thereby deprive the debtor and his creditors, not only of their property, but also of their right to work out a voluntary adjustment in their relations.

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36 *In re Reiman*, DC NY, Fed Case No 11,673 (1874); *Wright v Union Central Life Ins Co*, 304 US 502 (1938); *United States v Bekins*, 304 US 27 (1938); *Continental Ill N B & T Co v Chicago R I & P R Co*, 294 US 648 (1935); *Hanover Nat'l Bank v Moyses*, 186 US 181 (1902)

37 *Louisville Joint Stock Land Bank v Radford*, 295 US 555 (1935)

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When a creditor and his debtor enter into a contract creating the relationship, they make it subject to the bankruptcy power to modify it for the benefit and relief of the debtor, to the detriment of the creditor. That is a part of their contract. The power to take from the creditor for the benefit and relief of the debtor is within the "subject of bankruptcies."[38] But when the debtor-creditor relationship is created, they do not contract subject to any power of modification in favor of a stranger to the contract, to their mutual detriment, nor do they contract subject to any power of modification in favor of an unsecured creditor to the detriment of secured creditors. Conferring a benefit upon a stranger at the expense of creditors, or upon an unsecured creditor at the expense of secured creditors, is not within the "subject of bankruptcies."

Railroads are privately owned, even though their property be devoted to public use. This Court has held[39] that railroad property is

> "**** entitled to the protection of the Constitution, and in the precise manner in which protection is given. It can only be taken by the exercise of the power of eminent domain; and a condition precedent to the exercise of such power is *** that the statute conferring it make provision for reasonable compensation to the owner of the property taken."

The power of Congress to regulate interstate commerce is derived from Article 1, §8, Clause 3, of the Constitution. That power can only be exercised in subjection to the guaranty of due process.[40] In the cited case this Court said:

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38 *Louisville Joint Stock Land Bank v Radford*, 295 US 555 (1935); *Wright v Union Central Life Ins Co*, 304 US 502 (1938)

39 *Western Union Telegraph Co v Pennsylvania R Co*, 195 US 540, 570 (1904)

40 *Railroad Retirement Board v Alton R Co*, 295 US 330 (1935)

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"This court has repeatedly had occasion to say that the railroads, though their property be dedicated to public use, remain the private property of their owners, and that their assets may not be taken without just compensation. The carriers have not ceased to be privately operated and privately owned, however much subject to regulation in the interest of interstate commerce. *There is no warrant for taking the property of one and transferring it to another* without compensation, whether the object of the transfer be to build up the equipment of the transferee or to pension its employees." (295 US 357—Emphasis supplied)

Under the Commerce Clause, Congress has power to prescribe rules by which interstate commerce shall be regulated.[41] Nevertheless, the power of regulation is not absolute, but is limited by the constitutional guaranty that no person shall be deprived of his property without due process of law.[42]

Under no circumstances can the 5% bondholders' private property be taken in the manner and for the compensation provided. Even if taken for public use under the power of eminent domain, the Fifth Amendment requires the payment of just compensation, which must be made only and solely in money. All other proposed mediums of payment have been stricken down as unconstitutional.[43] And a taking which cannot be authorized under the power of eminent domain cannot be authorized under any other power.

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41 *Gibbons v Ogden*, 9 Wheat 1, 196 (1824)

42 *United States v Chicago, M St P & P R Co*, 282 US 311 (1931)

43 18 Am Jur, Eminent Domain, §128; 3 Nichols on Eminent Domain (3 ed) §8.2; 29 CJS, Eminent Domain, §191b; Lewis on Eminent Domain (3 ed) §§ 682, 756

If the 5% bondholders are to be deprived of their private property, the only method by which it can constitutionally be taken is by the exercise of the power of eminent domain. That great power authorizes a taking of private property for "public use," but does not authorize a taking in the "public interest,"[44] as the "forced merger" plan proposes.

Debtor has been judicially declared to be engaged in "public use."[45] Since it is already in public use as an operating railroad, the taking cannot be justified on the basis that debtor would be acquired for public use. Property devoted to one public use may be taken for a different and higher public use, but private property devoted to public use cannot be taken by another for the same public use.[46] The only purpose for which Coast Line seeks to acquire debtor is to continue to operate it for identically the same public use in which it is now being operated.

The end result of merger, consolidation or transfer would be to vest in Coast Line railroad property devoted to public use already, and Coast Line would operate it not for a different, but for the same, public use. The only real change would be that operating profits would thereafter inure to the benefit of Coast Line rather than debtor's 5% bondholders.

Courts of all jurisdictions have been impressively emphatic and uniform in holding that private property dedi-

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44 18 Am Jur, Eminent Domain, §37

45 *Florida East Coast Ry Co v Shaw*, 11 F2d 653 (1926)

46 18 *Am Jur, Eminent Domain*, §97; 1 *Nichols on Eminent Domain* (3 ed) §2.2(8); *West River Bridge v Dix*, 6 How 507 (1848); *Boston Water-Power Co v Boston & W R Corp*, 40 Mass 360 (1839); *Cary Library v Bliss*, 151 Mass 364, 25 NE 92, 7 LRA 765 (1890); *Lake Shore & M S Ry Co v Chicago & W I R Co*, 97 Ill 506 (1881); *Long Island Water Supply Co v Brooklyn*, 166 US 685 (1897—distinguishing between the State itself taking a public utility rather than another private corporation)

cated to "public use" cannot be taken for the same public use. This Court said at an early date:[47]

> "Nor could this bridge have been taken by the State, and kept up by it, as a toll bridge. This could not be called an appropriation of private property to public purposes. *There would be no change in the use, except the application of the profits,* and this would not bring the act within the power. The power must not only be exercised bona fide *** but the property, not its product, must be applied to public use.
>
> "It is argued that if the State may take this bridge, it may transfer it to other individuals, under the same or a different charter. This the State cannot do. It would in effect be taking the property from A to convey to B." (Emphasis supplied)

In *Elkins Elec R Co v Western Maryland R Co*[48] the District Court held:

> "It must be conceded that, where one railroad company has secured under its charter rights the right of way and built thereon its line of road and is using the same for public uses, the Legislature could not authorize the taking wholly thereof by another railroad corporation for a like public use."

In a case[49] wherein counsel argued that if property "has already been appropriated to public use, and is, in fact, in such use in the hands of one corporation, it cannot be rightfully taken (even by the authority of a statute to that effect) away from such corporation, for the purpose of subjecting it to the same public use in the hands of another corporation," the Illinois Supreme Court conceded that to be true, since

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47 *West River Bridge v Dix*, 6 How 507, 537 (1848)

48 163 F 724, 732 (1908), affirmed 186 F 1022 (1911), certiorari denied 223 US 725 (1911)

49 *Lake Shore & M S Ry Co v Chicago & W I R Co*, 97 Ill 506 (1881)

> "where the public use in question is *the same*, such taking would undoubtedly degenerate into a taking from one for the mere purpose of giving to another, which we hold (under our institutions) is not within the domain of legislative power." (Emphasis supplied)

The Supreme Court of Washington[50] held that property devoted to public use by a public service corporation

> "cannot be taken to be used for the same purpose in the same manner, as that would amount simply to a taking of property from one and giving it to another, without any benefit or advantage whatever to the public—an act which the legislature is powerless to authorize."

To like effect the courts of Oregon,[51] Texas,[52] Pennsylvania[53] and Massachusetts[54] have held that property devoted to public use may not be taken from the owner and delivered to another to be used for the same purpose.

This case is the first in which any section of the Bankruptcy Act has been construed as authorizing an unsecured creditor or stranger to expropriate the security underlying senior claims. That would be the effect of the "forced merger." It would permit the owners of senior liens to be deprived of their seniority without either the payment of their debt or the exercise of their right in equity, and under the mortgage, to a public foreclosure sale at which they may bid their debt.

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50 *Samish Boom Co v Union Boom Co*, 32 Wash 586, 73 P 670, 672 (1903); *Harbor Boom Co v Superior Ct Pac County*, 65 Wash 129, 117 P 755 (1911)

51 *Oregon Cascade R Co v Bailey*, 3 Or 164 (1869)

52 *Sabine & E T Ry Co v Gulf & I Ry Co*, 92 Tex 162, 46 SW 784 (1898)

53 *Sharon Ry Appeal*, 122 Pa St 533, 17 A 234, 9 Am St Rep 133 (1888); *Cleveland & P R Co, Petitioner*, 2 Pittsb R 348 (Pa, 1862)

54 *Boston Water-Power Co v Boston & W R Corp*, 40 Mass 360 (1839)

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Petitioners urge that the Fifth Amendment prohibits any such enlargement of the bankruptcy power. They submit that the cramming down of the proposed merger, consolidation or transfer, to permit Coast Line to take their property at a price which has never been determined to be its fair value, for compensation which is not payable in cash, would violate the Fifth Amendment.

Because Congress intended constitutional application of the cram-down provision, it should not be given the unconstitutional application proposed by the commission and court of appeals majorities.

5. The 1935 Amendments to §77 Do Not Authorize the "Forced Merger," Because the Inclusion in §77(e) of the Boyd Case "Fair and Equitable" Standard Requires the Retention of Creditors' Property Rights as in Equity Receiverships and Precludes Their Divestment by "Forced Merger."

Three basic rules apply in interpreting §77:

1. Reorganizations are not compositions.[55]

2. Reorganizations are intended to avoid, not foster, liquidations and thus are distinguishable from ordinary bankruptcies.[56]

3. "*** a proceeding under §77 is not an ordinary proceeding in bankruptcy. It is a special proceeding which seeks only to bring about a reorganization ***."[57]

Since reorganizations are neither ordinary bankruptcies nor compositions, the statutes authorizing them should not be interpreted as though they were. Section 77 must be

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55 *Case v Los Angeles Lumber Products Co*, 308 US 106 (1939)

56 *Reconstruction Finance Corp v Denver & R G W R Co*, 328 US 495, 506, 509 (1946); *Fidelity Assurance Assn v Sims*, 318 US 608 (1943)

57 *Continental Illinois N B & T Co v Chicago R I & P R Co*, 294 US 648, 676 (1935)

examined in the light of its purpose which, in at least one respect, appears unmistakably in the language used.

The inclusion in §77(e) of the Boyd case "fair and equitable" standard is a congressional command that in railroad reorganizations creditors shall retain, within their respective classes, all rights in the debtor's property that they would have had in an equity receivership. Retention of the property rights is inconsistent with their divestment by "forced merger." Since the two cannot stand together —retention and divestment—Congress expressly authorized retention, which, of necessity, forbids divestment by "forced merger."

The "full and absolute priority rule" of the Boyd case is made applicable to railroad reorganizations by the §77(e) provision that the plan must be "fair and equitable." The rule has been restated by this Court in clear and unmistakable terms:[58]

> "The rule of the Boyd Case 'protects the rights of senior creditors against dilution either by junior creditors or by equity interests.' ***
>
> "Unless that principle is respected, there will be serious invasions of the rights of senior claimants to the benefit of junior interests. The property of one group will be subtly appropriated to pay the claims of another while lip service is rendered the principles of priority."

Thus before any non-creditor, or creditor of an inferior class, can obtain or retain an interest in the reorganized debtor, any new securities offered the senior class of creditors must be "of a value equal to the creditors' claims."[59] The rule is that "junior claims can receive nothing until

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58 *Institutional Investors v Chicago, M St P & P R Co*, 318 US 523, 569, 570 (1943)

59 *Consolidated Rock Products Co v DuBois*, 312 US 510, 530 (1941)

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the senior claims receive securities of a worth or value *equal to their indebtedness.*"[60] (Emphasis supplied) It requires that "senior claims first receive securities of a worth *sufficient to cover their face and interest* before junior claims receive anything."[61] (Emphasis supplied)

In any construction of the language of §77 the primary consideration is the congressional intent pointedly evidenced by the inclusion in §77(e) of the full and strict priority rule of equity receiverships. That rule was not founded on empirical or utilitarian concepts growing out of the ravages of severe economic depression. The Boyd case was heard in November 1912 and decided in April 1913.[62] Its forerunners, dating back at least to 1868,[63] were decided over a wide range of business conditions.

The rule of the Boyd case was founded on *the property rights of creditors*,[64] as those rights were known and un-

60 *Reconstruction Finance Corp v Denver & R G W R Co*, 328 US 495, 517 (1946)

61 *Ecker v Western Pacific R Corp*, 318 US 448, 483 (1943). Of course, the stockholders of an insolvent corporation may buy back into the reorganized debtor—in effect re-purchase its ownership; but they cannot do so with contributions which are so inadequate as to dilute creditors' rights. Thus those who make necessary fresh investments may receive in return only participations reasonably equivalent to their contributions. (*Case v Los Angeles Lumber Products Co*, 308 US 106, 121, 122) But this does not apply to an inferior creditor class. They have never had any ownership interest subject to being "bought back."

62 A peak in the business cycle occurred in January 1913, following a low in January of 1912. The next business cycle trough did not occur until December 1914. *Historical Statistics of the United States, 1789-1945*, published by the Department of Commerce, at page 320.

63 "It has been stated, in all correctness, that the absolute priority doctrine is 'fundamentally conservative' and that it 'seeks to preserve our capitalistic system by protecting the investor so that the system will work.' Frank, Epithetical Jurisprudence and the Work of the Securities and Exchange Commission in the Administration of Chapter X of the Bankruptcy Act (1941) 18 N.Y.U.L.Q. Rev. 317, 340. In its insistence upon the strict recognition of traditional priorities, the absolute priority rule—as Professor Dewing has indicated—simply reiterates what the Supreme Court said as long ago as in that conservative era of Chicago, Rock Island & Pacific R. Co. v. Howard, [7 Wall 392 (1868)] 2 Dewing, Financial Policy of Corporations (4th ed. 1941) 1366, footnote o." 6 *Collier on Bankruptcy* (14 ed) p. 3872, n. 48.

64 *Northern Pacific R Co v Boyd*, 228 US 482 (1913); *Case v Los Angeles Lumber Products Co*, 308 US 106 (1939)

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derstood over the long history of equity receiverships.[65] They are the substantive rights of mortgage creditors summarized in *Louisville Joint Stock Land Bank v Radford*, 295 US 555, 594, 595 (1935).[66]

Congress wrote those substantive rights into §77 by including in §77(e) the Boyd case "fair and equitable" standard. In an opinion by Mr. Justice Douglas, this Court unanimously determined just what the sum total of those rights means in terms of equitable ownership of a debtor's property.[67] It was there decided that when creditors brought an involuntary bankruptcy proceeding to effect a reorganization plan enforcing the absolute priority rule, then —

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65 The determination of the mortgagee's "priority" in terms of vested property rights during the growth of the full and strict priority rule is well set out in the following quotation from Mr. Justice Brewer in *Kneeland v American Loan and Trust Co of Boston*, 136 US 89, 97-98 (1890): "Upon these facts we remark, first, that the appointment of a receiver vests in the court no absolute control over the property, and no general authority to displace vested contract liens. Because in a few specified and limited cases this court has declared that unsecured claims were entitled to priority over mortgage debts, an idea seems to have obtained that a court appointing a receiver acquires power to give such preference to any general and unsecured claims. It has been assumed that a court appointing a receiver could rightfully burden the mortgaged property for the payment of any unsecured indebtedness. Indeed, we are advised that some courts have made the appointment of a receiver conditional upon the payment of all unsecured indebtedness in preference to the mortgage liens sought to be enforced. Can anything be conceived which more thoroughly destroys the sacredness of contract obligations? One holding a mortgage debt upon a railroad has the same right to demand and expect of the court respect for his vested and contracted priority as the holder of a mortgage on a farm or lot. So, when a court appoints a receiver of railroad property, it has no right to make that receivership conditional on the payment of other than those few unsecured claims which, by the rulings of this court, have been declared to have an equitable priority. No one is bound to sell to a railroad company or to work for it, and whoever has dealings with a company whose property is mortgaged must be assumed to have dealt with it on the faith of its personal responsibility, and not in expectation of subsequently displacing the priority of the mortgage liens. It is the exception and not the rule that such priority of liens can be displaced. We emphasize this fact of the sacredness of contract liens, for the reason that there seems to be growing an idea that the chancellor, in the exercise of his equitable powers, has unlimited discretion in this matter of the displacement of vested liens."

66 *In re Utilities Power & L Corp*, 29 F Supp 763, 769 (DC Ill, 1939)

67 *Helvering v Alabama Asphaltic Limestone Co*, 315 US 179 (1942)

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"From that time on they had effective command over the disposition of the property." (315 US 183)

Thus, whether and to what extent §77 might have constitutionally modified mortgage creditors' rights, should not be a problem here. When the "fair and equitable" standard was written into §77(e) at least sufficient of the mortgage creditors' substantive property rights were preserved to assure their retention of "effective command over the disposition" of debtor's property.

A "forced merger" necessarily violates those substantive property rights. It would render futile and ineffective the equitable owners' command over the disposition of the property. It would susbtantially invade and violate the entire bundle of property rights preserved to equitable owners by §77(e). It would be in irreconcilable conflict with the full and absolute priority rule.

In the face of the explicit congressional inclusion of that rule in §77(e) no mere inference that Congress intended to permit a "forced merger" can prevail. There never has been, and is not now, any basis for reading any such inference into §77.

The insistence of Congress on the application of the full and absolute priority rule to railroad reorganizations forecloses any intention to permit a "forced merger." The very nature of a "forced merger" contemplates results permissible only under the composition or liquidation theories, but §77, like Chapter X, rejected the composition theory "in favor of the full priority rule of the Boyd case."[68] This was shown with sparkling clarity in *Case v Los Angeles Lumber Products Co*, 308 US 106, 119, footnote 14 (1939), which says:

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[68] *Marine Harbor Properties v Manufacturers Trust Co*, 317 US 78, 86 (1942); *Case v Los Angeles Lumber Products Co*, 308 US 106, 118 (1939)

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"The statutory scheme of § 77B (in those respects which are material here) is in sharp contrast to that which was provided for compositions under former § 12. This court said in Callaghan v. Reconstruction Finance Corp. 297 US 464, 470, 80 L ed 804, 809, 56 S Ct 519, 30 Am Bankr Rep (NS) 446: 'Reorganizations now permitted under § 77B present certain resemblances to compositions under § 12, which have been commented upon as supporting the constitutionality of the reorganization provisions of § 77 or § 77B . . . But § 77B contemplates a procedure and results not permissible under § 12. Reorganizations are nowhere referred to in the statute as compositions.' Under § 12(a) (as it existed at the time § 77B was enacted) only a 'bankrupt' could offer 'terms of composition to his creditors.' Under § 77B(d) plans may be proposed not only by the debtor but also by a designated percentage of the creditors or, where the debtor is not found to be insolvent, by a specified percentage of stockholders. Section 12(d) as it then existed provided that the judge 'shall confirm a composition if satisfied' inter alia that 'it is for the best interests of the creditors.' See Fleischmann & Devine v. Saul Wolfson Dry Goods Co. (CCA5th) 299 F 15, 4 Am Bankr Rep (NS) 1028. The 'fair and equitable' standard employed in § 77B was not then present in § 12. Consent by the debtor to the composition was implicit in former § 12 (cf. Re Bryer (CCA2d) 281 F 812, 49 Am Bankr Rep 32). But under § 77B approval of a plan by security holders who have no equity in the enterprise is unnecessary. Re 620 Church Street Bldg. Corp. 299 US 24, 81 L ed 16, 57 S Ct 88, 32 Am Bankr Rep (NS) 185. The general view was well expressed in Re Dutch Woodcraft Shops (DC) 14 F Supp 467, 469, 30 Am Bankr Rep (NS) 351. 'The preservation of business enterprises must not be at the expense of

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creditors, and the provisions of § 77B should not be taken advantage of to effect what, in fact, amounts to a composition under § 12.' "

Insistence by Congress on the full and absolute priority rule is established not only by the "fair and equitable" provision in §77(e) but also by the 1952 amendments to the Bankruptcy Act. By those amendments Congress wrote the rule out of the "composition" sections of the Act (Chapters XI, XII and XIII) but retained it in the reorganization provisions.[69]

That in the reorganization sections Congress also rejected the liquidation theory, whether by "forced merger" or otherwise, and rejected it in favor of the full and absolute priority rule, is established by *Fidelity Assurance Assn v Sims,* 318 US 608 (1943) and *Continental Ill N B & T Co v Chicago R I & P R Co,* 294 US 648 (1935).

The former was a Chapter X case but the principle decided applies here. This Court said (318 US 618):

"It is urged that a plan of liquidation may constitute a reorganization under Chapter X, and decisions

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69 "Sections 35, 43, and 50 of the bill make similar changes in sections 366, 472 and 656a of the act. These sections presently require a finding that a proposed plan under chapters XI, XII, and XIII shall be 'fair and equitable.' In fact, however, the fair and equitable rule, as interpreted in *Northern Pacific Railway Co. v. Boyd*, 228 U. S. 482, 33 S. Ct. 554, 57 L. Ed. 931 (1913) and *Case v. Los Angeles Lumber Products Co., Ltd.*, 308 U. S. 106, 41 Am. B. R. (N. S.) 110, 60 S. Ct. 1, 84 L. Ed. 110 (1939), cannot realistically be applied in a chapter XI, XII, or XIII proceeding. Were it so applied, no individual debtor and, under chapter XI, no corporate debtor where the stock ownership is substantially identical with management could effectuate an arrangement except by payment of the claims of all creditors in full.

"Chapter XI has replaced the old composition procedure under former section 12 of the Bankruptcy Act, where the fair and equitable rule did not apply. Nor is it practicable or realistic to apply the rule in a proceeding under chapter XI, XII, or XIII.

"The proposed amendment is designed to remove the fair and equitable provision, and by the paragraph added to each of the amended sections it is made clear that the rule of the *Boyd* and *Los Angeles* cases shall not be operative under those three chapters." Senate Report No. 1395 and House Report No. 2320, 82nd Congress, 2nd Session, paragraph No. 43 in each report.

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> are cited to that point, but an examination of them will demonstrate that in none save where the corporate purpose of the debtor was, in effect, holding and liquidating securities was the plan such as is proposed here. Under the facts of this case, the suggested plan is but an alternative for ordinary bankruptcy ***."

The latter was a §77 case. It was there said that "a proceeding under §77 is not an ordinary proceeding in bankruptcy" but "is a special proceeding which seeks only to bring about a reorganization."

It is utter nonsense to assert that a "forced merger" will or can safeguard the rights of equitable owners to the extent of the value of their security. Such a claim ignores the mechanics by which a "forced merger" must be produced; the considerations making it desirable to the covetous mergor but rightly objectionable to the mergee; and an ignorance of men and affairs consistent only with an anchorite's detached cogitations.

The key to the "forced merger's" necessary invasion of the mortgagee's property rights is that fundamentally the acquiring railroad dictates the terms of acquisition. The acquiring railroad being an outsider, or at best a member of an inferior unsecured creditor class, cannot be compelled by Court or Commission to acquire the debtor's property. Unless the Commission fixes bargain terms, the acquiring railroad can and will refuse to acquire.

The result cannot be whitewashed with a semantic juggling of the word "value," using terms correctly applied by this Court only to cases involving allocations or allotments among creditors—such as "equitable equivalence." The rule of full and absolute priority is not a rule of "equitable equivalence." It is a rule which enforces the legal and constitutional rights of the prior lien creditor.

The doctrine of "equitable equivalence" applies only to a creditor reorganization in which indebtedness is scaled down to bring it within ability to pay and new securities representing that ability are distributed to creditors in the order of their priority. It is a doctrine which applies only where there are overlapping and conflicting liens, and in marshalling it is necessary to give each lien its relative position in the reorganized debtor. It is not a doctrine which permits squeezing out a senior lien in the fashion here proposed. *Preble Corp v Wentworth,* 84 F 2d 73, 74 (CA 1, 1936) holding that "to take the property from the mortgagee upon an appraisal is an attempt to use a supposed or possible value, over and above the appraisal, for the benefit of other creditors and stockholders. If there is any such surplus value, it belongs to the first mortgagee, up to the amount of his debt."

The evil is not only that of the instant case—it is inherent in the "forced merger" process. This evil of acquisitor-Commission collaboration cuts as deeply as that of the bondholder-stockholder collaboration in the equity receivership cases, of which this Court said in the Boyd case (228 US 507):

> "The invalidity of the sale flowed from the character of the reorganization agreement regardless of the value of the property, for in cases like this, the question must be decided according to a fixed principle, not leaving the rights of the creditors to depend upon the balancing of evidences as to whether, on the day of the sale the property was insufficient to pay prior encumbrances."

CONCLUSION

On the basis of the facts and applicable law, petitioners urge that the judgment of the Court of Appeals should be reversed with directions to that Court to affirm Judge

Strum's order disapproving the so-called "forced merger" fourth plan of reorganization, or that the judgment of the Court of Appeals should be vacated and Judge Strum's order reinstated.

Respectfully submitted,

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APPENDIX A

Section 77 was added to the Bankruptcy Act by the Act of March 3, 1933, 47 Stat 1474, c 204. It was revised by the Act of August 27, 1935, 49 Stat 911, c 774. The controlling provisions, as enacted originally and as revised, are quoted below:

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"(b) A plan of reorganization within the meaning of this section (1) shall include a proposal to modify or alter the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include, in addition, provisions modifying or altering the rights of stockholders generally, or of any class of them; (3) shall provide adequate means for the execution of the plan, which may, *so far as may be consistent with the provisions of sections 1 and 5 of the Interstate Commerce Act as amended,* include the transfer or conveyance of all or any part of the property of the debtor to another corporation or to other	"(b) A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; *** (5) shall provide adequate means for the execution of the plan, which may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations, *** the sale of all or any part of the property of the debtor either subject to or free from any lien at not less than a fair upset price,

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corporations or the consolidation of the properties of the debtor with those of another railroad corporation, or the merger of the debtor with any other railroad corporation ***." (Emphasis supplied)	the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein ***."
"(d) *** Following such hearing, the commission shall render a report in which it shall recommend a plan of reorganization (which may be different from any which has been proposed) that will, in its opinion be equitable, will not discriminate unfairly in favor of any class of creditors or stockholders, will be financially advisable, will meet with the requirements of subdivision (g) of this section, and will be compatible with the public interest. *** Thereafter the plan of reorganization recommended by the commission shall be submitted in such manner as the commission may direct to the creditors and stockholders of the debtor for acceptance or rejection, together with the	"(d) *** the Commission *** shall *** hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subsections (b) and (e) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. *** The Commission, if it approves a plan, shall thereupon certify the plan to the court together with a transcript of the proceedings before it and a copy of

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report or reports of the commission thereon; and the commission may at the same time afford an opportunity to accept or reject any other plan of reorganization filed as in this subdivision (d) provided."

"(e) A plan of reorganization shall not be finally approved by the commission until it has been accepted in writing and such acceptance has been filed in the proceeding by or on behalf of creditors holding two-thirds in amount of the claims of each class whose claims or interests would be affected by the plan, and by or on behalf of stockholders of the debtor holding two-thirds of the stock of each class: *Provided, however,* That if adequate provision is made in the plan for the protection of the interests, claims, and liens of any class of creditors or stockholders in the manner provided in clauses (5) and (6) of subdivision (g), of this section, then the acceptance of the plan by such class of creditors or

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the report and order approving the plan. ***"

"(e) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice *** hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with

1933

stockholders shall not be requisite to the approval of the plan: *And provided further,* That the acceptance of stockholders shall not be requisite to the confirmation of the plan if (1) the judge shall have determined (a) that the corporation is insolvent, or (b) that the interests of stockholders will not be adversely affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan, and its stockholders are bound by such acceptance. *** Upon acceptance of the plan in accordance with the provisions of this subdivision (e) the commission may, without further proceedings, grant authority for the issue of any securities, assumption of obligations, transfer of any property, or consolidation or merger of properties, to the extent contemplated by the plan *consistent with the purposes of the Interstate Commerce Act as amended.* ***" (Emphasis supplied)

1935

the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; *** If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) hereof, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, *** *Provided,* That

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submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the equity of such class of stockholders has no value, or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any, or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance: *Provided further*, That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially

1933

"(f) If the plan recommended by the commission is accepted as provided in subdivision (e), the commission shall thereupon certify the plan to the court together with its approval thereof and that the same has been so accepted, together with a report of the proceedings before it and its conclusions thereon. If the plan accepted as provided in subdivision (e) differs from the plan recommended by the commission it shall, upon acceptance, be submitted to the commission, which shall hear all interested parties upon such notice and subject to such rules and regulations as it shall prescribe. If after such hearing the commission determines that the accepted plan

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in its opinion is equitable and will not discriminate unfairly in favor of any class of creditors or stockholders; will be financially advisable; will meet the requirements of subdivision (g) of this section; and will be compatible with the public interest; the commission shall thereupon certify the plan to the court, together with its approval thereof and that the same has been duly accepted, and together with a report of the proceedings before it and its findings and conclusions thereon. ***"

"(g) Upon such approval by the commission, and after hearing such objections as may be made to the approved plan, the judge shall confirm the plan if satisfied that (1) the approved plan complies with the provisions of subdivision (b) of this section, is equitable and does not discriminate unfairly in favor of any class of creditors or stockholders; *** (5) the approved plan provides, with respect to stockholders of any class the acceptance

1935

"(e) *** Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is

1933

of which is requisite to the confirmation of the plan, and who would not become bound by the plan under the provision of subdivision (h) of this section, and of which more than one-third have not accepted the plan, adequate protection for the realization by them of the value of their equity, if any, in the property of the debtor dealt with by the plan either by a sale of the property at not less than a fair upset price, or by appraisal and payment in cash either of the value of their stock or, at the objecting stockholder's election, of the value of the securities, if any allotted to such stock under the plan; (6) the plan provides with respect to any class of creditors the acceptance of which is requisite to the confirmation of the plan, and who would not become bound by the plan under the provisions of subdivision (h) of this section, adequate protection for the realization by them of the value of their securities, liens, and claims,

1935

required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: *Provided,* That, if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e). *** If it shall be necessary to determine the value of any property for any purpose under this section, the Com-

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either (a) by the sale of such property subject to their liens, if any, or (b) by the sale free of such liens at not less than a fair upset price, and the transfer of such liens to the proceeds of such sale, or (c) by appraisal and payment in cash of either the value of such liens and claims or, at the objecting creditors' election, the value of the securities allotted to such liens and claims under the plan. Section 57, clause (h), of this Act shall be applicable to the appraisal of securities under this section, and the value of the unpaid balance shall be appraised as an unsecured claim; and (7) the debtor, and every other corporation issuing securities or acquiring property under the plan, is authorized by its charter or by applicable State or Federal laws, upon confirmation of the plan, to carry out the plan. In the case of a sale or appraisal under clause (5) or (6) of this subdivision (g) the court shall refer to the com-

1935

mission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."

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1933

mission for its consideration and determination the amount to be fixed as the upset price and the appraisal of any securities."

"(h) Upon such confirmation the provisions of the plan shall be binding upon (1) the corporation, (2) all stockholders if the judge shall have determined (a) that the corporation is insolvent, or (b) that the interests of stockholders will not be adversely affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance, (3) all stockholders of each class of which two-thirds in amount shall have accepted the plan, (4) all creditors whose claims are payable in cash in full under the plan, (5) all creditors entitled to priority under subdivision (c) of this section, whose claims are not payable in cash in full under the plan, provided two-thirds in amount of such creditors shall have accepted the plan

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in writing filed in the proceeding, (6) all other unsecured creditors, provided two-thirds in amount of such creditors shall have accepted the plan in writing filed in the proceeding, and (7) all secured creditors of each class of which two-thirds in amount shall have accepted the plan. *** Upon confirmation of the plan by the judge, the debtor *and other corporations affected by the plan*, or organized or to be organized for the purpose of carrying out the plan, shall, subject to the jurisdiction of the Commission, have full power and authority to put into effect and carry out the plan and the orders of the judge relative thereto ***." (Emphasis supplied)

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judge relative thereto, under and subject to the supervision and the control of the judge ***. Upon confirmation of a plan the Commission shall, without further proceedings, grant authority for the issue of any securities, assumption of obligations, transfer of any property, sale, consolidation or merger of the debtor's property, or pooling of traffic, to the extent contemplated by the plan *and not inconsistent with the provisions and purposes of the Interstate Commerce Act as now or hereafter amended.* ***" (Emphasis supplied)

APPENDIX B

Section 5 of Interstate Commerce Act, as enacted by Transportation Act of 1920, Act of February 28, 1920, 41 Stat 456, c 91, codified in 49 USCA §5.

"§5. *Combinations and consolidations of carriers.* ***

"(4) *Consolidation of railroads into limited number of systems.* The commission shall as soon as practicable prepare and adopt a plan for the consolidation of the railway properties of the continental United States into a limited number of systems. In the division of such railways into such systems under such plan, competition shall be preserved as fully as possible and wherever practicable the existing routes and channels of trade and commerce shall be maintained. Subject to the foregoing requirements, the several systems shall be so arranged that the cost of transportation as between competitive systems and as related to the values of the properties through which the service is rendered shall be the same, so far as practicable, so that these systems can employ uniform rates in the movement of competitive traffic and under efficient management earn substantially the same rate of return upon the value of their respective railway properties.

"(5) *Tentative plan of consolidation; hearings; adoption and publication.* When the commission has agreed upon a tentative plan, it shall give the same due publicity and upon reasonable notice, including notice to the governor of each State, shall hear all persons who may file or present objections thereto. The commission is authorized to prescribe a procedure for such hearings and to fix a time for bringing them to a close. After the hearings are at an end, the commission shall adopt a plan for such consolidation and publish the same; but it may at any time thereafter, upon its own motion or upon

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application, reopen the subject for such changes or modifications as in its judgment will promote the public interest. The consolidations herein provided for shall be in harmony with such plan.

"(6) *Consolidation of railroads by agreement.* It shall be lawful for two or more carriers by railroad, subject to this chapter, to consolidate their properties or any part thereof, into one corporation for the ownership, management, and operation of the properties theretofore in separate ownership, management, and operation, under the following conditions:

"(a) *The proposed consolidation must be in harmony with and in furtherance of the complete plan of consolidation mentioned in paragraph (5)* and must be approved by the commission; *** (Emphasis supplied)

"(c) Whenever two or more carriers propose a consolidation under this section, they shall present their application therefor to the commission, and thereupon the commission shall notify the governor of each State in which any part of the properties sought to be consolidated is situated and the carriers involved in the proposed consolidation, of the time and place for a public hearing. If after such hearing the commission finds that the public interest will be promoted by the consolidation and that the conditions of this section have been or will be fulfilled, it may enter an order approving and authorizing such consolidation, with such modifications and upon such terms and conditions as it may prescribe, and thereupon such consolidation may be effected, in accordance with such order, *if all the carriers involved assent thereto,* the law of any State or the decision or order of any State authority to the contrary notwithstanding. (Emphasis supplied)

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APPENDIX C

Section 5 of Interstate Commerce Act, as amended by Transportation Act of 1940, Act of September 18, 1940, 54 Stat 898, c 722, codified in 49 USCA §5, pocket part supplement.

"§5. *Combinations and consolidations of carriers—Pooling; division of traffic service, or earnings* ***

"*Unifications, mergers, and acquisitions of control*

"(2) (a) It shall be lawful, with the approval and authorization of the Commission, as provided in subdivision (b)—

"(i) for two or more carriers to consolidate or merge their properties or franchises, or any part thereof, into one corporation for the ownership, management, and operation of the properties theretofore in separate ownership; or for any carrier, or two or more carriers jointly, to purchase, lease, or contract to operate the properties, or any part thereof, of another; or for any carrier, or two or more carriers jointly, to acquire control of another through ownership of its stock or otherwise; or for a person which is not a carrier to acquire control of two or more carriers through ownership of their stock or otherwise; or for a person which is not a carrier and which has control of one or more carriers to acquire control of another carrier through ownership of its stock or otherwise; or

"(ii) for a carrier by railroad to acquire trackage rights over, or joint ownership in or joint use of, any railroad line or lines owned or operated by any other such carrier, and terminals incidental thereto.

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"(b) Whenever a transaction is proposed under subparagraph (a), the carrier or carriers or person seeking authority therefor shall present an application to the Commission, and thereupon the Commission shall notify the Governor of each State in which any part of the properties of the carriers involved in the proposed transaction is situated, and also such carriers and the applicant or applicants (and, in case carriers by motor vehicle are involved, the persons specified in section 305 (e)), and shall afford reasonable opportunity for interested parties to be heard. If the Commission shall consider it necessary in order to determine whether the findings specified below may properly be made, it shall set said application for public hearing; and a public hearing shall be held in all cases where carriers by railroad are involved unless the Commission determines that a public hearing is not necessary in the public interest. If the Commission finds that, subject to such terms and conditions and such modifications as it shall find to be just and reasonable, the proposed transaction is within the scope of subparagraph (a) and will be consistent with the public interest, it shall enter an order approving and authorizing such transaction, upon the terms and conditions, and with the modifications, so found to be just and reasonable; Provided, That if a carrier by railroad subject to this chapter, or any person which is controlled by such a carrier, or affiliated therewith within the meaning of paragraph (6), is an applicant in the case of any such proposed transaction involving a motor carrier, the Commission shall not enter such an order unless it finds that the transaction proposed will be consistent with the public interest and will enable such carrier to use service by motor vehicle to public advantage in its operations and will not unduly restrain competition.

"(c) In passing upon any proposed transaction under the provisions of this paragraph (2), the Commission

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shall give weight to the following considerations, among others: (1) The effect of the proposed transaction upon adequate transportation service to the public; (2) the effect upon the public interest of the inclusion, or failure to include, other railroads in the territory involved in the proposed transaction; (3) the total fixed charges resulting from the proposed transaction; and (4) the interest of the carrier employees affected.

"(d) The Commission shall have authority in the case of a proposed transaction under this paragraph (2) involving a railroad or railroads, as a prerequisite to its approval of the proposed transaction, to require, upon equitable terms, the inclusion of another railroad or other railroads in the territory involved, upon petition by such railroad or railroads requesting such inclusion, and upon a finding that such inclusion is consistent with the public interest." ***

"Plenary nature of authority under section

"(11) The authority conferred by this section shall be exclusive and plenary, and any carrier or corporation participating in or resulting from any transaction approved by the Commission thereunder, shall have full power (with the assent, in the case of a purchase and sale, a lease, a corporate consolidation, or a corporate merger, of a majority, unless a different vote is required under applicable State law, in which case the number so required shall assent, of the votes of the holders of the shares entitled to vote of the capital stock of such corporation at a regular meeting of such stockholders, the notice of such meeting to include such purpose, or at a special meeting thereof called for such purpose) to carry such transaction into effect and to own and operate any properties and exercise any control or franchises acquired through said transaction ***."

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